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Politics this week

Aug 19th 2004
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Back from the brink

Reuters

Muqtada al-Sadr, the rebellious Shia cleric whose militiamen have fortified themselves in the Imam Ali mosque in Najaf, indicated that he might accept an offer to leave the shrine and turn his “Mahdi Army” into a political movement. The offer came from emissaries who had been sent from a “big tent” of politicians meeting in Baghdad to choose members of an interim parliament, which will help oversee progress towards elections in January. Iraq's interim government said again that if Mr Sadr did not lay down his arms, he and his men would be evicted by force.

See article

Ariel Sharon's plan to withdraw Jewish settlements from the Gaza strip suffered another setback. Members of the Likud party convention passed a resolution designed to prevent him from forming a coalition with the opposition Labour Party. Without the help of other parties, Mr Sharon would not have enough votes to push his Gaza plan through parliament.

See article

The UN said it was concerned by the lack of progress that **Sudan's** government had made in reining in the Arab militia that has driven 1.2m black Sudanese from their homes in the western region of Darfur. Sudan has two weeks to convince the UN that it is trying. The first contingent of 150 African Union peacekeepers arrived in Darfur, with a mandate to protect AU observers. Nigeria mulled sending 1,500 more.

Following a massacre of 160 Congolese **Tutsi** refugees in Burundi, Rwanda and Burundi threatened to send troops into Congo to crush genocidal Hutu militias there. One of Congo's vice-presidents, a Tutsi, threatened to quit government and take up arms to defend Tutsis.

See article

Switzerland decided to hand back to **Nigeria** $500m allegedly embezzled by the late dictator Sani Abacha and stashed in Swiss accounts. The Nigerian government estimates that this represents nearly a quarter of the money Abacha stole while in office between 1993 and 1998.

We do not recall

EPA

Venezuela's President Hugo Chávez won almost 60% of the vote in a recall referendum. The opposition claimed that the vote was rigged. International observers first said all was well but later decided to scrutinise the poll more closely.

See article

Henrique Meirelles, the president of **Brazil's** central bank, was accorded ministerial status in the country's government despite being under investigation for tax evasion. The opposition, which plans to challenge the decision, claims this is a ploy to make possible prosecution more difficult. Mr

Meirelles denies any wrongdoing. Meanwhile, Brazil's Supreme Court ruled in favour of a pension tax, a key element in the government's efforts to bolster the country's finances.

Colombia's government offered to release 50 jailed FARC rebels in exchange for hostages held by the left-wing guerrillas, reversing its previous policy on exchanges of captives. But the FARC still hold hundreds of people in Colombia's jungles.

Haiti's national football team played the Brazilian side in Port-au-Prince, the country's capital, to promote reconciliation. Earlier, one of the leaders of the rebel movement which forced the departure of former President Jean-Bertrand Aristide in February was acquitted along with a former police chief of a murder in 1993. The speedy trial was criticised by human-rights organisations and the United States.

See article

Troops out

George Bush announced a big shift in overseas **military deployments**. Up to 70,000 troops, almost a third of America's overseas fighting force, will be brought home gradually. The largest reductions are to come in Germany and South Korea; troop numbers in Iraq and Afghanistan will not be affected.

See article

James McGreevey, **New Jersey's** governor, said he would resign after admitting to an extra-marital affair with a man whom he employed as his adviser on homeland security. But he resisted calls to step down immediately.

See article

California's Supreme Court nullified 4,000 **same-sex marriages** that took place in San Francisco earlier this year and said that the city's mayor, Gavin Newsom, had defied current state law. But the court did not rule on the constitutionality of gay weddings.

See article

Residents of **Florida's** west coast mopped up after Hurricane Charley's 145mph winds swept through the region. At least 20 people were killed and the cost to insurers is estimated at around $7 billion.

See article

AP

Red or fed

Maoist rebels announced a blockade of **Nepal's** capital, Kathmandu. Drivers stopped bringing in food and other supplies, fearing reprisals. The rebels said the blockade would continue indefinitely.

A bomb, attributed to separatist terrorists, killed 18 people on **India's** independence day in the north-eastern state of Assam.

See article

Pakistan published a list of six “most wanted” al-Qaeda terrorists with a bounty of $1m on their heads.

Georgia on his mind

President Vladimir Putin of **Russia** blamed the **Georgian** government for the upsurge of fighting in the separatist enclave of South Ossetia. But he said Russia would do anything to “regulate and restore” Georgia's territorial integrity.

See article

Soren Jessen-Petersen, a Danish diplomat who has become the new UN governor of **Kosovo,** said after taking office there would be a “greater sense of urgency” about moves to resolve the province's final political status.

At least nine people died in heavy storms which swept through **France**, and in Paris, cemeteries and parks were closed for fear of falling trees. The government said rescue services were over-stretched because swimmers ignored warnings of heavy seas.

Hungary's ruling Socialist-Liberal coalition came under serious strain after the economy minister, Istvan Csillag, was sacked. The liberal SZDSZ party, a junior partner in the coalition, fiercely opposed the dismissal but stopped short of leaving the government.

Eight **British** men arrested in anti-terrorism raids two weeks ago were charged with conspiracy to murder, and plotting to use explosives, chemicals and radioactive materials. One was also charged with possessing plans of the IMF and other buildings.

See article

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Business this week

Aug 19th 2004
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Cut-price Google

The glamour began to fade for **Google.** The world's leading internet-search engine cut the number of shares on offer in its initial public offering and slashed the indicated price—valuing the firm at $23 billion rather than $35 billion or more—after muted interest from investors. Google also revealed that the Securities and Exchange Commission was investigating a breach of its regulations over an interview with its founders published in *Playboy*.

See article

Canadian police began a criminal investigation into the accounting practices of **Nortel Networks**, one of the world's leading telecoms-equipment makers. Nortel dismissed several senior executives in April as regulators began probing its accounts. The company paid millions in bonuses on inflated profits in 2003.

The costs of bankruptcy can be high. In **MCI's** case they are very high. Some 45 firms of lawyers and consultants are claiming over $600m at a New York court for guiding the phone company, previously known as WorldCom, out of Chapter 11 protection in April this year. A bankruptcy judge may yet decide to cut the fees.

A transatlantic partnership of four big buyout firms agreed to pay $3 billion for **Intelsat**, the world's second-largest satellite operator. Apax, Permira, Apollo Management and Madison Dearborn will acquire equal stakes in the Bermuda-based company. Two other satellite firms have fallen into the hands of private-equity groups this year.

As if dominating online auctions is not enough, **eBay** acquired a 25% stake in Craigslist, a cult online classified-advertising service that offers everything from jobs to car- sharing and sex in several American cities. Unusually, many of the adverts are run at no charge.

Driving away

DaimlerChrysler boosted its cash reserves by some $900m with the sale of its 10.5% stake in South Korea's Hyundai Motors, a relic of the car giant's ambitious plans for global expansion. DaimlerChrysler recently put the brakes on financial help for its struggling Japanese partner, Mitsubishi. It pledged to continue joint projects with the Korean firm.

US Airways, seeking to avoid Chapter 11 bankruptcy for the second time in two years, asked permission from America's tax authorities to reschedule payments to its pension plan. It needs to cut costs by some $1.5 billion over the next few months.

Air France and its subsidiary, **KLM**, followed the lead of British Airways and Lufthansa by introducing surcharges to pass the rising costs of fuel to customers. Meanwhile, BA offered more pay to check-in staff and baggage handlers to prevent a threatened strike.

Called to account

Parmalat launched lawsuits seeking $10 billion in damages against Deloitte & Touche and Grant Thornton, two auditing firms that for years oversaw the accounts of the bankrupt Italian dairy-product firm. It accuses them of improper auditing that allowed huge sums to be “stolen, squandered or wasted”

by former managers.

See article

A female employee of **Costco** filed a sex-discrimination lawsuit against the discount retailer seeking class-action status on behalf of up to 650 past and present workers. Costco is accused of denying positions in top management to women. Several of the lawyers involved are taking similar action against Wal-Mart.

In the pipeline

The **price of oil** surged to $47 a barrel this week after continued violence in Iraq exacerbated concerns about supplies and official figures in America showed a fall in crude stocks. But Hugo Chávez won a referendum confirming his tenure as Venezuela's president by a wide margin, which could end oil strikes organised by opposition leaders.

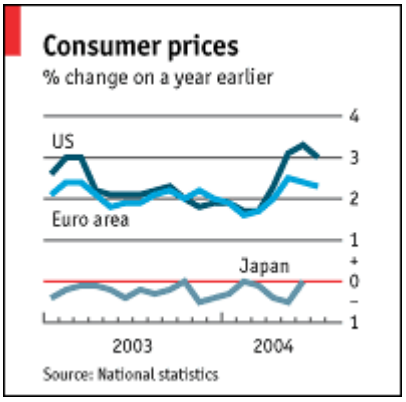
See article

Yukos, Russia's embattled oil firm, sold its half of Rospan, a gas joint-venture, to its partner, BP, for $357m, giving it some cash to help in settling a $3.4 billion tax bill. But a Russian court ruled against other asset sales by Yukos, and said that its tax bill must be paid by the end of the month nevertheless.

The American army swiftly retreated from a threat to withhold 15% of future payments to **Halliburton**, the Pentagon's biggest civilian contractor in Iraq. The company is to be given more time to answer claims that it overcharged for providing services to American troops in Iraq.

Deflated expectations

Consumer prices in America fell in July by 0.1%, the first decrease this year, after fuel prices dropped compared with the previous month. Inflation over the past year hit 3%, down from 3.3% in June, strengthening hopes that the Federal Reserve will not push up interest rates as much as had been thought.



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China

China's growing pains

Aug 19th 2004
From The Economist print edition

The dark side of China's stunning boom includes pollution and a collapsing state health-care system

IN THE old days, 25 years ago, life was straightforward in China. If you lived in a town, you worked in a state-owned factory or office. If you lived in the countryside, you worked on a collective farm. You didn't earn much, but that didn't really matter because there wasn't much to buy. Clothing options were largely limited to a choice of a dark grey Mao suit or a dark blue Mao suit. Only party officials got to use cars. For everyone else, private transport meant waiting months for the chance to buy a scarce Flying Pigeon bicycle.

In return for living a life of fathomless drabness, people's basic needs were reasonably well looked after. Health care (though it was, in truth, often seriously basic) was provided across the country by the state. Adequate pensions were provided in the same way. Housing was heavily subsidised, schooling was free. Of course, there were dramatic perturbations to contend with (the famine-inducing Great Leap Forward, the Cultural Revolution), but the arrangement had some clear benefits. China's performance on literacy, life expectancy and infant mortality was more characteristic of a middle-income country than a developing one, and hugely better than that recorded by similar-sized but democratic India. The system was sometimes called the iron rice-bowl, which sounded reassuring. The trouble is that most people want something a bit more exciting to eat than rice.

Those days, of course, are long gone. Since Deng Xiaoping launched his “open door” policy in 1978, China has witnessed probably the most dramatic burst of wealth creation in human history. Its income per head has increased sevenfold in that time: more than 400m people have been lifted out of severe poverty. Along its seaboard, and down the length of the Yangtze river, a middle class, perhaps 100m strong, has been created, where none at all existed before. Visit Shanghai, and you are visiting one of the most dynamic and cosmopolitan cities on earth. “To get rich is glorious,” Deng said, and everywhere people are doing just that.

The price of progress

But as with any vast transformation, there has been a price to pay. The state has retreated not just from agriculture—over 60% of China's population still live in the countryside—but from great swathes of industry and commerce, too. Inevitably, this has led to unemployment on a staggering scale. Reliable numbers are hard to come by, and the official ones are certainly gross underestimates. But there are perhaps as many as 15m unemployed in China's cities, and ten times that number in the countryside who have little or nothing to do. Still, this is at least a problem that rapid economic growth can be expected to chip away at fast. China's economy is clearly starting to slow, but an *Economist* poll of forecasts puts growth this year at 9.2%, and at a still-stellar 7.9% next. Other kinds of problem, however, will need imaginative policy changes to correct. This week, we look in detail at two of them.

As we report (see article), one casualty of the freeing up of China's economy has been its state health-care system, which has in effect collapsed. This threatens to undo one of the genuine achievements of which the Communist Party can boast: life-expectancy in parts of the country, particularly in the west, may actually now be falling. Diseases like tuberculosis and measles, which had been thought tamed, are making their return. Burdened by the costs of modernising its economy, but receiving only a modest tax take (it has risen from 12% to 18% of GDP a year, but that is not enough), the government's deficit has

been increasing. The health system has been a victim. Over the last 20 years, the share of health spending picked up by central government has roughly halved. Hospitals and clinics have been forced to up their fees, and most people no longer have state-owned work units able to pick up the tab. Health insurance barely exists outside the cities, so even a minor illness can easily push a family into appalling debt. This means that in some areas poverty is growing.

Pollution (see article) is an invariable consequence of development everywhere, but in China it is reaching scandalous proportions. The World Bank reckons that China is home to 16 of the world's 20 most polluted cities, and calculates that pollution and environmental degradation together cost China as much as $170 billion annually. Pollution is hardly new: Mao's drive for industrialisation created environmental catastrophes all over the country. But with the acceleration of economic growth, the problem has hugely worsened. Some of the forces at play have even served to undermine the state's efforts at curbing pollution. Local authorities now operate on a much freer rein than they used to, though without any sort of popular oversight. They have little incentive to make life difficult for employment-generating companies in their bailiwicks merely on the say-so of Beijing.

These, of course, are only two of the growing pains that afflict China as it continues its breakneck growth. A properly funded pensions system is sorely needed, with the withering-away of the state-owned enterprises that used to provide one. Cleaning up the banks could easily cost several hundred billion dollars. Yet look back at the industrial western nations of, say, 150 years ago, and it is worth remembering that none of these had pension systems, or state health care, and most of them had appalling pollution too—London's “pea-souper” fogs spring to mind. What enabled them to change was growth, coupled with muscular policymaking.

In China, the growth is plainly available, and there are clear signs that the government is starting to shoulder its new responsibilities too. As well as the grim tidings, there is good news in the battle against pollution. The courts have more teeth than they used to, and ordinary citizens are starting to make use of them. Spending on environmental protection has increased sharply, and foreign firms are being invited in to help the clean-up. Besides, as countries get richer, they tend to pollute less, building more chip plants and fewer steel mills. As for health, the respiratory disease SARS alerted the authorities to the dangers of a run-down health service, and various forms of health insurance are now being tested. The market, too, is stepping in, offering better and cheaper alternatives to the state-owned hospitals.

Still, solving these problems cannot be fast, easy or free of cost. One way or another, the government needs to claw back some of the gains that people have made in the boom years. Instinctively, people do appear to understand that in the new China, the ability to get rich carries greater individual responsibilities: the savings ratio has shot up to over 40%, one of the highest in the world. But as they are increasingly asked to pay—through higher taxes, medical fees and insurance premiums—for things the state used to provide, citizens will surely want a greater say in how their money is spent. China's Communist leaders may be on the way to tackling health care and pollution, but how they cope with growing calls for accountability remains to be seen. The courts, and increasingly-assertive media, can do a certain amount. But of democracy—the best form of accountability—there is so far not the slightest sign. Booming China has $470 billion of foreign reserves stashed away, and cash can soothe a lot of growing pain. But the demand for votes will grow.

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Oil prices

A crude awakening

Aug 19th 2004
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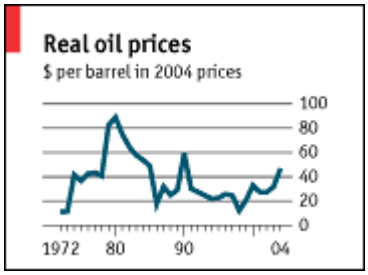
Never underestimate the power of oil



BRAIN power and computer chips are supposed to be the fuel of the modern "knowledge economy" rather than oil. Yet the black stuff still has the power to shock. Crude oil prices surged to a record $47 a barrel this week, nearly $10 higher than at the end of June. There are already signs that the economies of America, Japan and China are slowing. Could higher oil prices once again push the world economy into recession?

The optimistic camp claims that oil no longer matters much. Others, however, blame higher oil prices for the sharp slowdown in American consumer spending this year. In different ways, both are wrong.

Optimists rightly argue that higher oil prices should have a less-severe impact than in the past, partly because developed economies use only half as much oil per dollar of real GDP as they did in the mid-1970s. Moreover, the rise in oil prices has so far been relatively modest. Prices this week were two-thirds higher than their average level over the past four years. In each of the previous three oil shocks, oil prices tripled. After adjusting for inflation, oil prices are only half their peak in 1980.

Most economic models confirm that the recent rise in oil prices should have a relatively modest impact on output. A recent joint study by the IEA, the OECD and the IMF concluded that a sustained $10 a barrel rise in price would reduce global output by 0.5% after one year. If prices stay around their current level, rather than return to the average of the past four years, then almost one percentage-point might be wiped off global growth. That is not insignificant, but so far not enough to trigger a global recession when world GDP has been growing by almost 5% over the past year, its fastest for two decades.

Excuses, excuses

America's economy should, in theory, be hurt even less by higher oil prices than Europe's or Japan's, because America is also an oil producer, so its oil imports are smaller. Yet many commentators, including the Federal Reserve, have been quick to blame the higher oil price for the sharp slowdown in American consumer spending, which grew by an annual rate of only 1% in the second quarter, down from 4% average growth over the four previous quarters. But even in gas-guzzling America, spending on energy is not big enough to account for such a sharp slowdown. Goldman Sachs estimates that higher oil prices shaved only half a percentage-point off consumer spending in the second quarter. A more important explanation is that incomes are no longer being inflated by tax cuts as in the past three years, and "cash outs" from home-owners taking out bigger mortgages have tumbled.

The truth is that America's economy has started to sputter for reasons that have little to do with dearer oil, which proves the oil-price alarmists wrong. But that, in turn, means that America—and hence the world economy—is now more vulnerable to oil prices than the optimists and their standard economic models suggest. Those economists who blame the softness of consumer spending on oil prices seem to assume that this is a temporary blip, and spending will rebound once oil prices fall back to normal levels. But such thinking could be flawed on two grounds: part of the rise in oil prices may prove more persistent than in the past; and the slowdown in consumer spending may be due to deeper structural problems.

Oil prices have been partly buoyed by short-term worries about production in Iraq, Russia, Saudi Arabia and Venezuela. However, movements in forward prices (for delivery in the future) suggest that the

market expects oil prices to stay high for some time (see article). Unlike previous jumps in the oil price, caused by sudden supply disruptions, the current increase is due mainly to stronger demand. The increase in global oil consumption this year is likely to be the biggest for almost 30 years, largely thanks to China, and supply is tight because there has been little investment in new oil. If incomes continue to grow rapidly in China and other emerging economies, global oil demand will remain strong.

America, the world's biggest oil consumer, may therefore need to adjust to permanently higher oil prices. At the same time, by blaming America's slowdown on oil prices, economists are ignoring the fact that once consumers' diet of generous tax cuts and falling interest rates ended, it was inevitable that their spending would wobble. Massive fiscal and monetary stimulus has helped to support the American economy, but only at the cost of bigger economic and financial imbalances. America has literally been borrowing from future consumption. So higher oil prices now matter, not because they will themselves deliver a fatal blow to world economic growth, but because they come at a bad time, precisely when America's consumers are being forced, as was inevitable, to save more and spend less.

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Russia

A matter of Russian honour

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Vladimir Putin should solve rather than stoke regional conflicts

AFTER a humiliating decline as a world power, Russia is working hard to regain respect and authority. That is a fair, even praiseworthy aim. But to achieve it, Russia must respect other countries too, including places once ruled from Moscow. It will prosper more with friendly, confident countries around it—not weak, frustrated ones. Russia understands that, but often seems incapable of showing it.

By offering unconditional support to rebel regimes in the Georgian provinces of South Ossetia and Abkhazia, Russia dishonours itself and destabilises its neighbourhood (see article). Since South Ossetia broke away from Georgia 12 years ago, it has degenerated into a smugglers' paradise. Russian soldiers prop up a sleazy regime that peddles vodka and arms. Moves by Georgia to cut this illegal trade have led to a violent summer. Heavier fighting, and open Russian intervention, are a risk.

The crisis needs delicate handling, but the fundamentals are simple. South Ossetia is not a viable state. It lives on crime. Its government needs to be closed down as part of a generous settlement which Georgia now offers. Abkhazia, Georgia's other breakaway province, is a tougher problem, and its local government even less legitimate—in that it speaks for even fewer of the region's lawful residents—than South Ossetia's.

Of the two places, Abkhazia has more claim to separateness—and it was the scene, in 1992-93, of a war where both sides fought dirty. Any settlement must include some deal for Georgians who fled Abkhazia; but only a limited right of return may be possible—and not straight away. On the positive side, Georgia wants to talk, and will offer Abkhazia any arrangement short of independence. But by underwriting the separatists, Russia is holding up such a solution.

Faced with this, America and Europe should give more help to Georgia's Mikhail Saakashvili, whose openness to ethnic co-existence and western values make him the region's most promising leader for decades; the governments of the West should steady his hand while affirming his choices.

They should also look beyond Georgia, to other “frozen conflicts” in the region. One is in Moldova, where another rebel statelet, Transdniestria, lives on smuggling and Russian guns. Then there is a far bigger stand-off: over Nagorno-Karabakh and its environs, where a decade ago Armenians broke free from Azerbaijan and expelled local Azeris. That logjam has other causes besides Russian meddling—but it would be easier to shift if Russia worked constructively with the West.

All these conflicts destabilise countries on the new borders of NATO and the European Union. The four Russian-backed statelets at the heart of these disputes have something in common: they have no legal existence, and can easily serve as a free-for-all for illegal activity of every kind.

That should be a worry for Russia too. If it sponsors adventurism and racketeering in Georgia and Moldova, that is partly because its policy there has been captured by crooks. The West should take its worries to the top, putting it to Vladimir Putin in plain language. Will the president continue backing separatist regimes that live on smuggling? Is a miserable bit of local power worth the harm done to Russia's name as a responsible state? Of course it is not. But only when Mr Putin takes a stand will the behaviour of more lowly Russians change. And he will do so only if other countries persuade him that his reputation, and that of Russia, are at stake.

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Journalistic privilege

Blaming the messengers

Aug 19th 2004
From The Economist print edition

The Plame affair in America raises questions about the freedom of the press

UNLESS the American courts reverse themselves, the sight of journalists behind bars will no longer be confined to the world's worst regimes and the pages of George Orwell. There may soon be a spate of such sightings in the land of the free.

Last week, a federal judge sentenced Matthew Cooper, a reporter for *Time* magazine, to jail. Mr Cooper had refused to identify the White House officials who told him last summer that Valerie Plame, the wife of a whistleblower in the Niger uranium scandal, was an undercover CIA agent (see article). Mr Cooper will be imprisoned unless his appeal is upheld, and two other journalists who also received the leak have been subpoenaed and could face prison.

Should the journalists reveal their sources? Or should, on the other hand, judges put them behind bars for not doing so?

On the scribes' side, the first amendment to America's constitution, which guarantees freedom of the press, was designed to protect individual expression such as Mr Cooper's reporting. In practice, such reporting is put in danger by subpoenas. If reporters were routinely forced to identify confidential sources, those sources would dry up and the public would lose potentially valuable information. The public should not want the media to be servants of the legal system any more than it wants them servants of government. Moreover, federal and state laws exempt lawyers, doctors, therapists, priests and spouses from testifying in cases where they are in a position of trust in relation to the defendant. Why not journalists as well?

Indeed, 31 American states protect journalists by offering a limited legal privilege: reporters can be subpoenaed only if the evidence sought is essential and otherwise unobtainable. In practice, this privilege is generally observed. But clearly it also needs qualifying. Who is a journalist? Do bloggers count? Define “journalist” too narrowly, and free speech is unacceptably restricted; define it too broadly, and any witness to a crime can simply sign up as a freelancer to avoid testifying. There is also the problem of the information journalists receive. If a reporter is told, off the record, of an impending terrorist attack, journalistic immunity could not outweigh saving lives. The question then becomes which crimes are serious enough to trump reporters' privilege. Purist journalists might say none of them. Lawyers would argue that the courts should decide.

The media must, however, recognise that behind such high-flown arguments lies also self-interest, which can itself give rise to public scepticism. A powerful motive for reporters to protect their sources is the personal desire to be trusted by future sources, whoever they may be—even in cases when it is in the public interest for the sources to be unmasked. That is surely the situation in the Plame case. The evidence sought from the journalists is something the public might well want revealed: the identities of the Bush operatives who leaked Miss Plame's name. For their assault on the credibility of Miss Plame's husband was not only politically motivated but wilfully irresponsible. It seriously endangered all Miss Plame's intelligence contacts, and some may have died as a result. In the nature of spookery one cannot know, and any such damage has already been done. But it cannot be in the national interest for such leaking to go unpunished, for otherwise it could well occur again.

A case of competing public interests

In their own interests, the subpoenaed journalists are probably right to keep quiet, even though they are the only witnesses to a serious crime. The public will suffer from that decision, because the crime will thus go unpunished, but it can comfort itself with the fact that it gains overall from reporters' keenness to protect their sources, through the freer flow of information. In the end, the real loser may well be George Bush. For if no officials are to be punished for this crime, either by the courts or by their employer, then some voters will surely add it to their reasons for meting out their own punishment on another judgment day: November 2nd.

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About sponsorship

Israel and the Palestinians

A big man on a tightrope

Aug 19th 2004
From The Economist print edition

Can Ariel Sharon really evacuate the Jewish settlements in Gaza?

AP

Get article background

THE inner workings of Israeli democracy are notoriously impenetrable. Not for the first time, however, the future of the Middle East is about to be decided by the machinations of the country's fractious parties. On August 18th, Ariel Sharon's plan to evacuate all Jewish settlements in the Gaza strip and some in the northern West Bank bumped into another hurdle as his Likud party convention rejected the prime minister's plan to bring Labour into his governing coalition. Without more supporters inside his tent, Mr Sharon may not be able to muster the parliamentary majority he needs to implement his plan. But over recent months this proposal for “unilateral disengagement” has become virtually the only hope of breathing life into the moribund peace process with the Palestinians. Has the Likud now snuffed the last hope out?

Not necessarily. Mr Sharon's behaviour towards his party has come to resemble his behaviour towards the Palestinians: he hears their objection and ploughs on regardless. This week's vote was the third time a party institution has tried to check him. Two years ago the central committee rejected his endorsement of the idea that the Palestinians should be allowed a state alongside Israel. In May 2004, a party referendum voted down his Gaza plan, compelling him to bring a diluted version for cabinet approval. The current defeat makes clear that Mr Sharon lacks his party's support, despite his popularity with the general public. But he has once again vowed to ignore the convention and forge ahead.

Whether he will succeed is an open question. One threat he has brandished at his rebels is the prospect of an early general election, in which some of them might lose their jobs. But with a mandate that does not expire until November 2006, he is bound to see that as a last resort. Going to the polls earlier may force him into a challenging contest with the finance minister, Binyamin Netanyahu, the party's darling. Besides, it is the party that would draw up the list of candidates for parliament, and in its present mood it would probably produce a list even less favourable to quitting Gaza.

Since this week's vote was non-binding, Mr Sharon will probably prefer to batter his way through without an election. He can take comfort from the knowledge that Likud members of parliament are less hostile than the party activists. In a crisis, he might be able to muster a majority on the Knesset floor by calling on the support of parties that are not formally part of his coalition. But there are limits to how far any democratic leader can continue to function without party support, and Mr Sharon—for all the breathtaking ability of this burly man to walk a tightrope—is approaching this position.

As Israelis hold their breath, it is time for the outside world to adjust its thinking about Mr Sharon. He will never be the toast of the peaceniks. He is the architect of the settlement policy that has made it so bitterly hard for Israel to extricate itself from the Palestinians; he bears some of the blame for triggering the present violence by his provocative eve-of-*intifada* walk on Jerusalem's Temple Mount; his view of what a Palestinian state should look like is still very far from what the Palestinians want and deserve. As Israel's left likes to say, the right are slow learners. But Mr Sharon does seem at last to have learnt that Israel cannot hold on to all the land it conquered in 1967, and is risking all by beginning the process of withdrawal. That is why the settlers are determined to defeat him—and why he deserves the world's support.

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Letters

Aug 19th 2004
From Economist.com

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Winning the human race

SIR – Let us create a relationship between athletes and companies, as in Formula One motor racing, that combines the greatest talents with the best innovators ("Drugs and the Olympics", August 7th). A Dwain Chambers/GlaxoSmithKline team would compete against a Tim Montgomery/Pfizer team. The benefits would be large: drug safety would be enhanced, as a big firm could not risk the bad publicity of long-term harm to athletes; it would create the spectacle of "super-humans" capable of running 100 metres in four or five seconds; and innovations would be fast-tracked into the public domain. Who would not want a drug that could make them faster, fitter and stronger if it had no negative side-effects?

Phil Dunne
London

SIR – Gene-doping poignantly alludes to an ethical controversy that is at the root of all discussions on performance enhancement. Where and how do we draw boundaries between humans and super-humans? Which would we prefer to watch in competition? Which would we prefer to be?

Jonathan Suk
Edinburgh

SIR – To allow doping is to allow winners to be decided by the resources of chemists rather than the talent of athletes themselves. If the identity of the fastest man on the planet is to be determined by technological support, then it might as well be determined on motorbikes.

Matthew Wakefield
London

SIR – I do not share your pessimism about ridding sport of drugs. The World Anti-Doping Agency exists to protect an athlete's fundamental right to participate in drug-free sport and thus promote health, fairness and equality. To say that this is a hopeless task and that athletes should be allowed to take drugs or not as they wish is defeatist. It is not in the spirit of fair play either: a defining characteristic of sporting endeavour, which is what the Olympics is all about.

Ian Blackshaw
International Centre for Sports Studies
Neuchatel, Switzerland

SIR – Your comparison of doping chemicals to other "performance-enhancing" drugs is problematic. Drugs such as Viagra are intended for the use of those with a health problem. Even if healthy people use them, we can be a little more sympathetic to those who fool a partner for a few hours than to those who fool history with chemically enhanced world records.

Alper Bahadir
New York

SIR – One sport in America already has a liberal regime towards drugs with no detriment to the sport overall. Racehorses are permitted to take, for various ailments, drugs that often have side-effects that

enhance performance on the track. Most racing-form guides indicate which drug a horse is taking. Adopting such a system across human sports might be cumbersome but it would at least help the average fan make the same decisions as punters at the track.

Rob Luke
Carbondale, Illinois

Pakistan against terror

SIR – You ask why America considers President Pervez Musharraf "a bulwark against Islamic extremism. But many others do not" ("Winning the battle, not the war", August 7th). Those who do not appreciate Mr Musharraf's efforts fail to realise the true nature of contemporary terrorism. It is not something that can be banished with a magic wand; even the best and most sincere efforts can at times have patchy results. Impatient academic analysts must realise that winning the war on terrorism, and not just the battle, will be a long haul requiring a careful balancing of strategy and tactics.

Moreover, the accusation that Mr Musharraf "continued to indulge the mullahs in numerous ways", including allowing them to gain control of two of Pakistan's four provinces, is ludicrous. The Muttahida Majlis-i-Amal, an alliance of religious parties, gained control of the two provinces on the basis of its electoral performance and not because Mr Musharraf wanted it.

Javed Akhtar
High Commission for Pakistan
London

Spreading the word

SIR – Your article on "open access" to scientific literature is shockingly one-sided ("Access all areas", August 7th). As with most utopian visions it contains fatal flaws. Open access depends upon payment for all costs of publication by the author, or the supporter of the research, to replace the income currently made from subscribers. In many countries, government would become the principal source of funds for science publication. This sets up a system that can be politically controlled. Will researchers be allowed to publish politically incorrect work in subjects ranging from embryos to global change? Will interference such as forbidding co-authorship with residents of the state's enemies, as happens in America under the guise of financial sanctions, become the norm?

An author-pays model is also likely to lower overall quality, as publishers who are willing to sacrifice quality for profit lower standards to gain market share. There will be a reduction of useful access because we will all be scavenging in a huge garbage heap. There are disciplines, notably mathematics and some areas of theory, that are not funded well enough to support a non-subscription model of publication. It may be easy to find money in a large space or medical programme but what about the lone scientist working in his garret?

Do we really believe that a new economic model for science publishing should be legislated? Or should it be grown from the best that the scholarly community can do within its own marketplace? Much is being done within the current system to enhance distribution for scientists worldwide and to reach the public. These goals require much more than open access.

Fred Spilhaus
Executive director
American Geophysical Union
Washington, DC

Mind your language

SIR – Anybody with some knowledge of Central Europe would know that English is not spoken in the region ("After Babel, a new common tongue", August 7th). The language they speak there is American. English has been on the decline for a long time, even more so than German and French.

Anders Pape Moller
Orsay, France

SIR – As Willy Brandt, a former German chancellor, once remarked: “If I am selling to you, I speak your language. If I am buying, *dann müssen Sie Deutsch sprechen*.” Will the native English speakers take notice of his advice?

Cosmin Smeu
Ottawa

SIR – The European Court of Justice uses French only as its working language because at the time of the court's inception, French was a common denominator. But this linguistic regime does not necessarily correspond to the present situation. It may be time for change, even if it means a challenge for the staff of the courts and for the judges. Ultimately, the quality of justice itself is at stake.

Joakim Swedenborg
Trier, Germany

ONLINE ARTICLES

The following correspondence refers to articles published only online

George W. Putin

SIR - In your article on Russia's welfare reforms, “For richer or for poorer?” (Global Agenda, Economist.com, August 9th), you write: “That is in line with the general trend of Mr Putin's federalism, which has been to put more of the burden for services on to the regions whilst concentrating more power and supervision at the federal level.”

Were you not struck by the irony that Mr Putin's policy mirrors that of the Bush administration?

Jim Satterley
DeLand, Florida

Capital letter

SIR - In “The pros and cons of capital flight” (Global Agenda, Economist.com, August 13th) you mention that “the politicians and their flunkeys tend to fly back to their constituencies at the end of each week's parliamentary sessions, leaving (purpose-built capitals) half-deserted.”

That in itself is not a problem. It is the mandarins not moving among the constituents at the weekend (or any other time), and therefore not knowing what problems the populace at large must deal with, that is the real cause for concern. Let us consider the hypothetical problems of transport in, say, Melbourne and Seoul. Public servants in Canberra will organise interdepartmental study groups to examine the problems in Melbourne. They will then evaluate the study programme, cross-reference and legitimise responses, authenticate the results, and any other amount of dilly-dallying. Public servants in Seoul, on the other hand, will fix similar problems rapidly, if only because such problems interfere with their own interdepartmental study groups.

James Miller
Hangzhou, China

Tricks of the trade

SIR - Your report on the WTO's recent stitch-up “Progress at last, but still a long way to go”, (Global Agenda, Economist.com, August 2nd) notes some loopholes in the framework agreement, but still concludes that it entails the rich countries “paying a price” by reducing domestic support for agriculture. They are doing no such thing.

By itself, America's trick of redefining counter-cyclical payments as less trade-distorting (and thus

allowable) raises its permitted support from the current $39 billion to $49 billion annually. And in the absence of a proper definition of what is allowed under the “green box”, or of “non-trade-distorting” support, we are sure to see more creative redefinition on both sides of the Atlantic to protect existing programmes. This is no breakthrough; it is business as usual: developing countries and other agricultural exporters trading real concessions for illusory gains.

Aaron Cosbey
International Institute for Sustainable Development
Winnipeg, Canada

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About sponsorship

China's health care

Where are the patients?

Aug 19th 2004 | BEIJING
From The Economist print edition

Imaginechina

Health care and the environment have been overlooked in China's rush to capitalism. We look at health care below; at pollution in this article

Get article background

RONGRONG was only a few weeks old when her parents noticed swellings. They took her to a village clinic and to a rural hospital. Both failed to spot that the baby was severely malnourished, though they charged the equivalent of two and a half months of her father's income as a brick-factory worker. The delay probably cost Rongrong her life. When her parents eventually took her to a city hospital, where a correct diagnosis was made, she was in a critical condition. After seven days, and another three months' salary-worth of hospital bills, she was dead.

The baby, from a village in the central province of Anhui, was one of at least 200 infants around China who were seriously malnourished, and in some cases killed, by consuming substandard milk powder in the past few months. Parents had no way of knowing that the cheap but well packaged product they were buying was illegal and hardly more nourishing than water. And because of the prohibitive cost of health care, parents often failed to get their children treated in time to save them.

After the scandal came to light in April, the government announced that affected children would be treated free (the Chinese press has since reported that some hospitals resumed charging after the departure of the central government officials sent to investigate). Rongrong's parents, like other bereaved families in the area, received compensation from the local government. The payout of 12,000 yuan ($1,450) was the equivalent of nearly two years' income for Rongrong's father.

But the tragedy had taken its toll on Rongrong's mother, who now needs medical treatment herself. To have more time to look after her, her husband has given up his job at the brick factory and returned to subsistence farming. His wife's hospital bills have already amounted to more than three months' worth of his former salary.

Criticism of the affair has focused on the ubiquitous sale of fake and substandard products. But just as big a failing was that of the health system itself. The families who bought the milk powder were mostly poor country people. Undoubtedly fewer lives would have been lost if they had had better access to basic health care.

Mao Zedong, for all his egregious faults, would have done better at providing it. In his day, nine out of ten country people had access to subsidised health clinics run by the much celebrated “barefoot doctors”. But in the course of China's relentless march towards capitalism in the past two decades, this arrangement has collapsed. In the countryside, 90% of the population now has no health insurance. In the cities, nearly 60% are uncovered. Out-of-pocket spending on health care is soaring.

When the World Heath Organisation (WHO) ranked the public-health systems of 191 countries four years ago, China was placed at 144, behind some of Africa's poorest. India, which has half China's GDP per head, came in at 112. The criteria included fairness of access to health care and fairness of contributions to the cost.

Better to live on the coast

Judged by life expectancy, infant mortality and child-birth deaths, China's record looks impressive. Twice as many children in India die in the first few months of life, and twice as many mothers die in childbirth. At birth, Chinese girls can be expected to live to 73 and boys to 70—a level comparable to medium-level developed countries. But there are huge disparities between regions. In richer areas, such as around Shanghai on the coast, health indicators are as good as they are in many western countries. In western China, they are those of a basket-case country.

After making strong gains in the first three decades of Communist rule, health indicators have changed little in the past quarter-century, despite the extraordinary economic achievements of China, with annual average GDP growth of 9.7% in the past 20 years. Some health experts believe that in parts of the country—particularly in the west where incomes are half the level of the booming eastern seaboard—life expectancy might even be falling.

According to the World Bank, China has lifted 400m people out of severe poverty in the past two decades. But millions have slipped back into it as a result of health-care costs. Millions of others are dying because they cannot afford health care. A government survey three years ago found that some 60% of rural residents avoid hospitals altogether because of the expense. Diseases once declared tamed, such as tuberculosis, measles and snail fever, have been making a comeback. And amid the disarray of the system, a new infection, HIV, is rapidly taking hold.

Things could get much worse. In the coming years, the customary Chinese way of dealing with expensive medical crises—borrowing from family and friends—will become more difficult as the proportion of elderly citizens in the population rises steeply. The UN predicts that by 2040 China will have only two working-age people for every person over 60, compared with 6.4 in 2000.While ageing populations are common in the developed world, the Centre for Strategic and International Studies said in a recent report that China may be the first major country to grow old before it becomes rich.

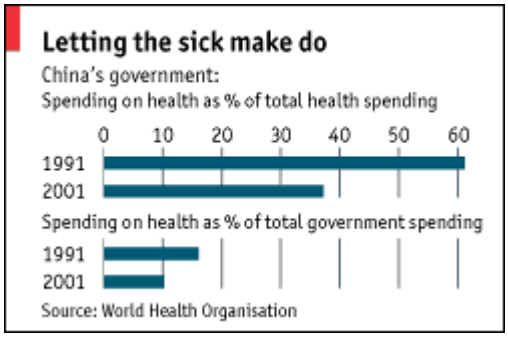
Too nervous to spend

Public anxiety over the collapse of affordable health care is reflected in China's high savings rate. Despite the parlous state of China's state-owned banks, bank savings by individuals have grown rapidly in recent years. Worries about the fast-rising costs of health care and education—and the lack of private-insurance schemes and other low-risk investment opportunities that might help offset them—are restraining consumer demand and thereby imperiling China's long-term economic growth.

This makes health-care reform a crucial part of China's development strategy. To ease growing pressures on its fragile financial system, China wants to become less dependent on government investment as an engine of growth. But unless consumers feel confident that they can cope with the risk of a serious health problem (as well as with all the other increasingly costly contingencies), it will be difficult to encourage them to spend.

Last year's outbreak of severe acute respiratory syndrome, or SARS, not only concentrated the government's attention on the problem but aroused the world's attention to the potential health threats from a country with a patchy record on epidemic control. Fortunately, SARS never took hold in the rural areas where facilities are the shabbiest. Had it done so, it would have been

hard to stop its spread.



Well into the crisis, the government realised this and tried to reassure people that they would not have to pay for any SARS treatment costs. But given the high possibility that SARS-like symptoms might turn out to be caused by another ailment not covered by free treatment, there was the likelihood that many people would have avoided the hospitals anyway.

The outbreak demonstrated how fragile and threatening the health system had become. Suddenly, officials began to turn their attention to neglected health problems such as HIV. China estimates that it could have around 1m HIV carriers at present. The WHO says this could rise to 10m by the end of the decade. Last year, for the first time, top leaders, including the prime minister Wen Jiabao, were shown on television shaking hands with AIDS patients. Officials, at least in some areas, have begun to overcome their prudishness and to promote condom use and the distribution of clean needles to drug addicts.

For President Hu Jintao and Mr Wen improving health care has also become part of a political strategy aimed at salvaging the Communist Party's badly tarnished image. Mr Wen and Mr Hu now stress the need to address the concerns of the marginalised. In 2002, the party set a goal of turning China into a middle-income country with a “well off” population by 2020. But in recent months the emphasis has shifted from simply increasing GDP per head to achieving broader measures of wealth, such as enjoying good health.

But getting there will be far more difficult than fulfilling GDP growth targets. For the past 20 years, the government's financial commitment to health care has been declining. Urban hospitals, though mostly still state-owned, now receive only about 10% of their operational funds from the state. For the rest they have to generate their own revenues, mostly from selling medicine and medical tests (the cost and wilful over-prescription of which is the biggest grievance of patients).

Even immunisation isn't free

Rural hospitals are in even worse financial shape. The most basic ones are run by governments at the township level, the lowest tier of government hierarchy. For most of these administrations, the only source of funding is the trickle of income they receive from higher-level government, plus taxes and fees that they raise from farmers and businessmen. Even preventive medicine now has to rely on fees. The WHO says that China is the only country in the western Pacific region which relies on patients to finance childhood immunisations. Not surprisingly, many peasants now avoid such treatment.

State-owned enterprises once shouldered much of the responsibility for basic health care, including the running of their own hospitals. But with the collapse of many such businesses, workers have been left to fend for themselves. Private businesses are supposed to pay for medical insurance, but most do not bother.

The chronic underfunding of public health has created a culture of cynicism and corruption in China's hospitals. As well as having to pay up front before they are treated, patients frequently complain that in order to get good treatment they need to pay “red packets” (bribes) to doctors and nurses.

In the past year—goaded by the SARS outbreak—the authorities have stepped up their efforts to ensure that country people and the poor get access to basic health care. In the countryside, they have designated more than 300 counties (about 10% of the total) where a new “co-operative medical system” is being tried, with a plan to make it countrywide by 2010. Funding is shared between voluntary participants, the local authorities and the central government. In addition, a new insurance scheme, paid for by central and local governments, has been introduced for the poorest of urban and rural families to cover the cost of serious illnesses. The scheme is due to be implemented nationwide next year.

But both projects have serious drawbacks. Local governments are often unwilling to make the necessary contributions, especially in poorer areas. And individuals are often unwilling to pay for a service they feel they may not immediately need. For the past two decades, local governments have gouged farmers for contributions to an almost non-existent health-care system, with the money being used mostly to pay staff (many surplus to requirements or simply non-existent, with the money being used to line officials' pockets) rather than to pay for services. Consequently, there is reluctance to join any new scheme.

Can market forces provide the answer?

What other options does China have? Some officials, seeing the market as the panacea, suggest that the government should withdraw entirely and let prices be controlled by competition. In recent years, many township governments have sold off or leased their hospitals to private investors. But while in some cases the investment may have helped improve conditions, there is little evidence that the price of health care has fallen.

In the cities, a few hospitals have been built with private money, and businesses have taken over some of the hospitals that used to be run by state-owned enterprises. By 2005, state enterprises are supposed to cease their support for all hospital facilities. Some hospitals will be closed, others merged with bigger ones or sold off.

Privatisation remains controversial. Two years ago the central government tried to limit the trend by decreeing that every township must retain at least one state-owned hospital. But many cities have pressed ahead with their own reforms without explicit approval from Beijing.

Xinxiang, a city in the central province of Henan, has engaged in the biggest sell-off, and one of the most controversial. Earlier this year it sold majority control of all of its five main hospitals to a single state-owned pharmaceutical company, China Worldbest Group. The government was happy to have reduced its health-care burden, and the Shanghai-based company was happy to have guaranteed outlets for its drugs. But what about competition? Many health-care specialists saw the move as the replacement of one overpriced monopoly by another, and the Shanghai government banned further such deals between drug companies and hospitals.

But there are signs that the central government is at last trying to adopt a more coherent policy for health-care reform. In early April, at its annual national conference on health-care issues, the Health Ministry circulated a secret draft of a policy paper outlining the respective roles of the government and the private sector in urban health care. Experts familiar with the document say it suggests that the government retain control of the main hospitals, but let second-tier hospitals be owned and operated privately. One expert estimated that this could involve the privatisation of 60% of urban hospitals. This would allow the government to increase its spending on the hospitals it keeps, thus reducing their financial dependence on charges for medicine and tests.

On the face of it this sounds a good idea. China's problem is not a shortage of medical facilities. It has a relative abundance of them: 1.6 doctors per 1,000 people compared with 0.4 in India, and 2.4 hospital beds per 1,000 people compared with India's 0.8. But this means that official resources are stretched too thin. Concentrating on key hospitals would enable the government to pay doctors a decent wage (though Chinese sources say that the document does not promise this will happen). At present a hospital director earns about the same as a company sales representative with a couple of years of experience. No wonder doctors are demoralised.

But if large numbers of people are still unable to afford treatment, such reforms will create a better system only for the affluent. In the long run, what China needs most is a health-insurance system that works. This should include insurance for private treatment (now non-existent), giving patients a bigger choice of facilities and stimulating private investment in hospitals. It would also need to ensure that those who contribute little or nothing to the system still get some coverage. In other words, the government needs to spend a lot more, particularly in the countryside and among rural migrants to the cities.

One reason why China's health-care system is in such a mess is that the central government's share of tax revenue has dropped in the past 20 years. But relying on local governments to do more will not work. At the township level, the majority are bankrupt. The central government needs to allocate more of its own money—and to force provincial governments (which like to go their own way fiscally) to make sure the allocations reach their intended targets.

Strong incentives, such as tax breaks, will be needed to encourage private business to run hospitals on a not-for-profit basis. Although there has been considerable interest among foreign and domestic private investors, very few large-scale investments have been made because of regulatory uncertainty and questions over profit and pricing. The establishment of a handful of foreign-run hospitals in the big cities for the rich and well-insured are rare exceptions. In poor areas, including much of the countryside, the government will need to remain the primary provider.

Achieving this will involve changing priorities. Prestige projects may have to be abandoned. And there will have to be a fairer allocation of resources to address the current imbalance by which cities currently enjoy 80% of health resources despite having only 35% of the population. And to make sure it all works, there will need to be an effective system of oversight which China now sorely lacks. The idea of good corporate governance is novel enough in China, but in health care it is non-existent. A sea change is needed in everything from hospital management to the way central and local governments spend their money. Even so, slowly and reluctantly as it may be, China is beginning to discover that market forces alone cannot produce good health care.

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America's troop deployments

Moving on

Aug 19th 2004
From The Economist print edition

Getty Images

Keeping fewer troops abroad may be clever thinking—or dangerous folly

Get article background

ARE George Bush's plans to cut the numbers of troops in bases overseas the shake-up America's armed forces need? Or are they a dangerous bit of politicking? Politics certainly influenced Mr Bush's timing. His announcement that, over the next decade, some 60,000-70,000 of the more than 200,000 American soldiers, sailors and airmen serving in permanent bases overseas would be pulled back home was made at a veterans' convention in Cincinnati, and there was no need to say anything at all this early. But the president's political advisers no doubt hope that “bringing more troops home” will stick in voters' minds, even as he insisted that those serving in Iraq and Afghanistan would stay as long as needed.

Two days later, before the same audience of veterans, the Democratic hopeful, John Kerry, struck a very different note. The redeployment would undermine relations with America's allies, he argued, and send the wrong signal to its enemies.

Campaign fisticuffs aside, the Pentagon's review of America's global military commitments has been going on virtually since the administration took office. Donald Rumsfeld, the defence secretary, wanted to take advantage of new technologies that enable troops to move more quickly to trouble-spots, and fight more effectively once they are there. The September 11th attacks brought even greater pressure to put more of America's overseas forces closer to the real threats. And the strain on the army from operations in Iraq has concentrated minds on how to make best use of the troops available.

Mr Kerry would rather recruit another 40,000 soldiers to cope with the problem of overstretch. All the same, it makes little military sense to keep America's overseas forces in the two great clumps, in Europe (chiefly in Germany) and Asia (chiefly in Japan and South Korea), that formed during the cold war to deter the Soviet threat. America now needs a more globally integrated military structure, able to move forces quickly to any trouble-spot. The plan is for numbers to come down faster in Europe, but the backwash of the changes will be felt most keenly in Asia.

Europe currently plays host to 114,000 American troops (down from over 300,000 at the end of the cold war) and over ten years will see the number drop to 72,000. Smaller changes will take place throughout

Europe, but Germany will lose its two American heavy divisions, while gaining a much smaller but more mobile brigade. The net effect: 40,000 troops would still be based there, compared with over 70,000 today. A snub after the recent political strains over Iraq? Both sides flatly deny it. America will also keep its huge Ramstein airbase, to rotate troops on to the Middle East and other hot spots.

A threat, then, to NATO? The alliance is undergoing its own streamlining of commands, and many of its officials think the reorganisation could go further. Most members have also accepted the need for reforms that will help turn out more capable and deployable soldiers of their own, though few have also agreed to pay for this. Mr Bush's planned military reorganisation may encourage them.

American officials accept that, despite long months of consultation, some allies are still nervous. But in Europe and elsewhere the reorganisation will help America build new defence relationships with countries such as Bulgaria and Romania, and in strategically important places like Central Asia, as troops rotate in for shorter tours in less permanent training facilities. It remains to be seen, though, whether this lighter “footprint” will be enough to reassure new allies (and some old ones) of America's continuing commitment.

In Asia, by contrast, the threats are still looming, and the planned cuts in overall numbers correspondingly smaller. But why cut at all? Pointedly, Mr Kerry asked this week how it can be safe to withdraw 12,000 American troops (actually 12,500, out of 37,000) from South Korea by the end of next year, just as America is negotiating with a hostile and probably nuclear-armed North Korea. Last week 3,500 combat troops were redeployed from South Korea to Iraq, suggesting that strains elsewhere have been having an effect.

Yet the bulk of the draw-down on the peninsula will come from cutting support services that can just as easily be provided from elsewhere. The decision already taken to move American bases away from Seoul and the front line with North Korea, it is argued, will actually strengthen America's ability to help defend South Korea. So will the extra $11 billion already earmarked for military improvements there. Putting more heavy bombers on Guam, and possibly moving an aircraft-carrier battlegroup from the Atlantic to the Pacific, will enable America to respond swiftly and forcefully to any attack. All the same, the South Korean government has asked for a two-year delay in the withdrawal.

In Asia, as in Europe, America will also be seeking new places to train, berth its ships and land its aircraft. Can Mr Bush do all this and save money, as he claims? Much depends on Congress, which will decide which bases to close and which to expand at home for returning troops and their families to use. Like the reorganisation overseas, that will take a lot of bipartisan co-operation—a tall order in any year, with or without an election.

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Gay marriage

Fear the counter-attack

Aug 19th 2004 | WASHINGTON, DC
From The Economist print edition

State initiatives banning gay marriage have got activists jumping

AP

Get article background

SLAPPING down San Francisco's mayor, Gavin Newsom, California's Supreme Court has left several thousand married couples unmarried. On August 12th the judges ruled that more than 4,000 marriage licences, issued by Mr Newsom in February and March, were “void and of no legal effect”.

Mr Newsom argues that a state law, which defines marriage as between a man and a woman, violates both state and federal constitutions. That issue is expected to be raised later this year in a lower court in San Francisco. For now, the city's gay and lesbian couples are in limbo.

Opponents of same-sex marriage have been fighting back ever since a ruling last November, when the Massachusetts Supreme Court legalised such marriages in the state. State lawmakers have passed an amendment to their state's constitution to ban gay marriage, though it must go to the voters in 2006. And there is still talk of an amendment to the United States constitution to ban gay marriage altogether, though one attempt has already failed in the Senate.

For gays, the most alarming aspect of the counter-attack is the drive to amend 12 state constitutions so that they define marriage as being only between a man and a woman. Conservative groups, citing the fear that other states will copy the “judicial activism” of Massachusetts, have put a constitutional amendment on the ballot in Arkansas, Georgia, Kentucky, Louisiana, Mississippi, Montana, Oklahoma, Oregon and Utah; North Dakota, Ohio and Michigan are expected to follow.

Technically, the ballot initiatives will not change much. In all these states, save Oregon, statutes already bar gays from marrying. But their adoption would still set back the movement for gay marriage by making it a dead issue in several more states. Though 39 states have laws that define marriage as between a man and a woman, so far only five—Alaska, Hawaii, Nebraska, Nevada and most recently Missouri—have bothered to amend their constitutions. An amendment makes it nearly impossible for gays to fight for marriage rights in the state courts, and also prevents gay-marriage activists from proposing state laws to change the statutes.

Gay-rights groups would then have few options apart from taking the fight to federal courts. Many are reluctant to do such a thing. They fear that any attempt to get a federal court order forcing a state to legalise gay marriage could have the opposite effect, providing tremendous momentum for the proposed federal ban on gay marriage.

Consequently, campaigns have been launched to fight the initiatives. All the votes, except Louisiana's, will coincide with the November 2nd election, and gay-rights groups are accusing the Republicans of trying to use the issue to turn out conservative voters.

Whether or not this is true, will the initiatives prevail? If Missouri's vote, at a primary election on August 3rd, is any guide, they will pass handily: Missourans backed the amendment 71% to 29%, even though gay activists greatly outspent their rivals. The primary was unusual in that an unpopular sitting governor was fending off a rival for his party's nomination, and that could explain the high turnout. But even if

Missouri was exceptional, the fight will be tough: opinion polls show that 56% of Americans oppose gay marriage against 32% who favour it.

Still, a clean sweep by the anti-gay-marriage camp is by no means a foregone conclusion. The initiative stands on shaky ground in left-leaning Oregon, where a judge upheld roughly 3,000 gay marriages that were performed in April, and where same-sex partners of state employees can claim benefits. Many gay couples whose marriages were recognised already call Oregon home.

Michigan and Ohio are not shoo-ins either. Conservative groups have made the initiatives in these two states particularly sweeping: they want the constitution to say that marriage between a man and a woman will be the only union recognised by the state. This would mean that no state institution would be able to grant special status to unmarried couples of any kind.

Shades of gay

What should California's Supreme Court have done about San Francisco's gay marriages?, %

	Total	18-24	25-44	45-64	65+
Voided the marriages and forbidden any more:	50	*33*	*46*	*55*	*65*
Allowed the marriages to stand, but forbidden any more:	7	*6*	*7*	*7*	*8*
Allowed the marriages to stand, and allowed such marriages to continue:	30	*49*	*31*	*27*	*20*

Governor James McGreevey [of New Jersey] resigned because he had concealed the fact that he was gay. What do you think?, %

	Total	18-24	25-44	45-64	65+
He should have resigned:	38	*30*	*32*	*43*	*51*
He should not have resigned:	47	*55*	*50*	*44*	*39*

Source: *The Economist*/YouGov. Poll of 1,799 adults conducted nationally August 16th-18th

Gay-marriage activists have seized on this strong language to appeal to voters who might be affected. They have also argued that such a change would hurt the economy. Michigan and Ohio, already two of the worst-hit states in terms of job losses, might become unattractive to mobile firms if benefits given to the unmarried partners of employees no longer had any protection in the courts.

Could an image of intolerance on the issue of gay marriage hurt the conservative cause more generally? Perhaps, in the long run. The young are much more in favour of the idea than the old. But in the near term, the gay-marriage issue could help Republicans if the vote is close. In Ohio, for example, evangelical Christians account for a quarter of the population and are not, as a rule, great voters. Yet they could come out to defeat gay marriage and, while they are at it, vote for Mr Bush.

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New Jersey politics

McGreevey's bombshells

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Out of the closet, but still in office—just

IT TAKES a lot to shock New Jersey. The home of “The Sopranos” has at least three ex-mayors in jail, and is plagued with corruption from top to bottom. Nevertheless, on August 12th, jaws dropped. “I am a gay American,” declared the Democratic governor, James McGreevey. Then, with his wife smiling tightly by his side, he admitted to engaging in an extra-marital affair with a man, and said he would resign.

At first, friends and foes alike felt sorry for him: a twice-married father of two, struggling with his sexuality and looking “deeply into the mirror of one's soul”. But it soon emerged that Mr McGreevey's confession may have been a clever political tactic, preventing Golan Cipel, a former aide, from filing a sexual-assault and harassment lawsuit against him. And the announcement also diverted attention from the real reason why he is stepping down.

Mr McGreevey appointed Mr Cipel to head the state's Homeland Security Department on a salary of $110,000 a year, even though he is an Israeli and had no security clearance. News reports revealed that Mr Cipel demanded $50m and then $5m to stay quiet about their relationship. Thickening the plot, Charles Kushner, Mr McGreevey's close friend and top moneyman, sponsored Mr Cipel when he first arrived from Israel. Earlier this summer, Mr Kushner was charged with hiring prostitutes to silence a witness in a fund-raising investigation. New Jersey is wondering what on earth will come out next.

The governor has had a tumultuous term. He has been dogged by fund-raising scandals. A former top aide was charged with insider-trading. His former police superintendent has a criminal record. On top of all this, New Jersey's bishops announced in May that Mr McGreevey, a Catholic, would no longer be given communion because of his pro-choice position on abortion, his support of stem-cell research, and the fact that he had been divorced without getting an annulment.

You would think he couldn't wait to escape. Yet Mr McGreevey vows not to step down until November 15th. Under New Jersey law, if the governor were to leave by September 3rd, more than 60 days before this year's general election in November, the state would hold a special election to decide who would serve the last year of the term. Since the governor is the only statewide elected official, he has no elected successor.

At present Richard Codey, head of the state Senate, is set to serve the remainder of the term. Unsurprisingly, Republicans are calling for the governor to step down immediately, and now even Democrats are beginning to agree. They are worried that the longer Mr McGreevey stays, the more he will taint the party.

Many state Democrats had hoped for a replacement in Jon Corzine, New Jersey's senior senator and a former head of Goldman Sachs. But Mr Corzine said on August 18th that he will not be seeking a special election. Besides, he may feel his future lies elsewhere, as a possible treasury secretary if John Kerry wins the White House. Mr Corzine may be one of the few New Jerseyans who will not mind if Mr McGreevey stays until November.

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The electoral week

On the trail

Aug 19th 2004
From The Economist print edition

A man called horse

“He does have a long narrow face. But a lot of his face is in his jaw. So I would not say he has a Marfanoid face. It's ironic that people are putting this false story out there when you consider Cheney's very real health problems.”

Dr Mary Roman, of New York Presbyterian Hospital, on speculation that John Kerry has Marfan syndrome. New York Daily News, August 16th

Fish have feelings, too

“We've been inundated with calls. People are outraged.”

William Rivas-Rivas, of People for the Ethical Treatment of Animals, after George Bush gave a fish he had just caught to his dog to play with. Washington Post, August 13th

The Schwarzenegger Factor (1)

“He and I both married up. He married a woman who was a member of the other party, I married a woman who was a member of the other party...And Arnold has massive biceps, and I have massive hair.”

Mr Kerry campaigning in California. Washington Times, August 13th

The Schwarzenegger Factor (2)

“I'm also proud to be here with the governor of California. He's a—because he and I share a lot in common. We both married above ourselves, we both have trouble with the English language, we both have big biceps—well, two out of three aren't bad.”

Mr Bush campaigning in California, August 12th

Mea culpa

“See, I thought we were going to find stockpiles. So did everybody else, you know. We haven't found them yet, I recognise that.”

Mr Bush, in Oregon, admits that he was wrong about Iraqi weapons. Washington Post, August 16th

Protesters of the week

During the Republican Party convention in New York, protests will include 100 women draped in American flags and wearing anti-

Republican “protest panties” performing a “mass flash”, while Paul Revere imitators will ride bicycles down Lexington Avenue shouting “The Republicans are coming! The Republicans are coming!”

Time, August 23rd

Ken for First Man?

“It allows girls to think about turning Barbie's dream house into the White House. Since Barbie is such a large part of girls' lives, we believe it's important to encourage them to become tomorrow's leaders, and Barbie for President sends that message.”

Marie Wilson, of the White House Project, which encourages women to stand for elected office, on the doll's presidential campaign. Business Wire, August 12th

Eurotrash

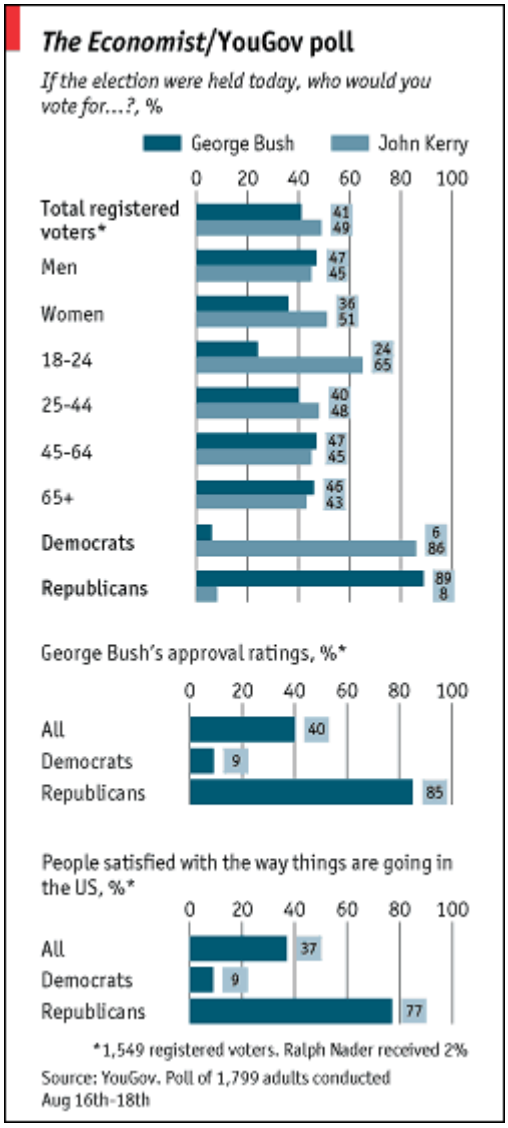
“It is via this [his mother's] family that the Democratic candidate is descended from Henry II, the king of England and father of Richard the Lionheart.”

Burke's Peerage links John Kerry to royalty. Associated Press, August 16th

Talk dirty to me

“John would whisper French phrases in my ear...I don't know what he was saying. I don't speak French.”

Lee Whitnum, once a girlfriend of John Kerry. New York Daily News, August 18th



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The Valerie Plame affair

Go to jail

Aug 19th 2004
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The journalists, not the leakers, are made to pay the price

WHEN Joseph Wilson, a former American ambassador, alleged in July 2003 that President George Bush had falsely accused Iraq of trying to buy uranium from Niger, the president's men fired back. Two White House officials called at least six Washington journalists and told them that Mr Wilson's wife, Valerie Plame, was an undercover CIA agent who had worked in Niger, thus suggesting Mr Wilson was a stooge for the WMD-shy CIA.

Robert Novak, a syndicated columnist, took the bait and identified Miss Plame as a covert operative, attributing the information to “senior administration officials”. Leading Democrats quickly noted that Mr Novak's sources had probably violated a law forbidding government officials from knowingly revealing an undercover agent's identity to an unauthorised person, and called for them to be outed and jailed. But the first people to face prison are not the leakers, but the journalists who reported the leaks.

Last week, the grand jury investigating the case subpoenaed Judith Miller, a reporter for the *New York Times*, in an attempt to learn who had blown Miss Plame's cover. The newspaper will try to quash the subpoena, but is unlikely to succeed. The judge who will hear the motion, Thomas Hogan, has just rejected a similar motion by *Time*'s Matthew Cooper, who had written a story confirming Mr Novak's account and was previously subpoenaed in the case. Mr Hogan subsequently held Mr Cooper in contempt of court, which is punishable by up to 18 months' imprisonment, and said he will fine *Time* $1,000 a day until Mr Cooper reveals his sources, although the penalties will not be imposed until an appeal is heard. Prosecutors have subpoenaed at least three other journalists. It is not known whether Mr Novak himself has been called to testify.

The Plame case puts Mr Bush in a political bind. If prosecutors continue to subpoena journalists, he will appear to be an enemy of the first amendment to the constitution, which guarantees freedom of the press. If the authorities back off, he will be vulnerable to charges that he is whitewashing a case with security implications.

The Plame affair is not the only recent example of prosecutors threatening journalists with jail time. According to a survey by the Reporters Committee for Freedom of the Press, the average news organisation received 2.6 subpoenas in 2001. And although 31 states have laws insulating journalists to various degrees from the obligation to reveal their sources, the Supreme Court ruled in 1972 that the first amendment does not relieve reporters of the requirement to testify in federal criminal cases. The Justice Department has non-binding guidelines requiring that information sought from journalists be “essential to a successful investigation” and unavailable from other sources. But the Plame case meets that standard: the only witnesses to the crime were the journalists who received the leaks.

Mr Cooper is likely to push his appeal to the Supreme Court, but the court declined to hear the most recent appeal of a “newsgatherer's privilege” case—from Vanessa Leggett, an author who spent 168 days in jail for refusing to disclose sources. And the precedent it set in 1972 leaves little legal wriggle- room. Barring a major reversal by the court, it seems that the only protection journalists will have is prosecutors' disinclination to go after them.

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Hurricane Charley

Tough, in an uninsured mobile home

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AP

Florida weathers its second-costliest hurricane

ALTHOUGH four people died in Cuba and one in Jamaica, Florida took the worst of it. The city of Punta Gorda was devastated; 20 Floridians were killed, and at one point the winds reached 145 miles an hour. Cartographers will have to redraw their maps, because Captiva Island (where Hurricane Charley made landfall in Florida on August 13th) is now Captiva Islands; the skimpy sandbar was cut in two.

The damage to insured homes, cars and businesses is estimated at $7 billion or so. Only Hurricane Andrew in 1992, with $15.5 billion in insured losses, was costlier. Since Punta Gorda was a town where thousands of mostly elderly people were living in uninsured mobile homes, the dollar value of the damage will never be exactly known.

President George Bush toured the area on August 15th, promising the residents of the state and his brother, Governor Jeb Bush, that federal financial help is on the way. The Federal Emergency Management Agency has declared 25 of Florida's 67 counties disaster areas; they include the seven counties with most of the state's citrus groves, where 90,000 people work.

Hurricane Andrew led to a spree of price-gouging by petrol-station owners and insurance agents. This time, people have been told to demand to see insurance agents' licences, and toll-free telephone numbers have been set up for people to call if they suspect that they are being scammed.

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Red alert

Aug 19th 2004
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New York is about to play host to an alien species

IN THE last week of August, New Yorkers will leave their city in droves. This is not because they fear that the Republican convention will provide a lure for terrorists. The real reason is an even greater fear: meeting a Republican.

Although America has two large political parties, each with about half of all eligible voters, New York City falls almost entirely into the Democratic camp. One in eight voters registers as Republican and, despite the meagre number, this vastly overstates their significance. Only three of the 51 city council members are Republican, plus two of 65 state assembly members and one of the 14 congressmen. Staten Island, the city's smallest borough, is perceived by the rest of the city to be a Republican refuge, but even in this stronghold they amount to little more than one-third of the voters.

This antipathy toward Republicans is not new. Since the second world war, Republicans have sent to the White House two George Bushes, Ronald Reagan, Gerald Ford, Richard Nixon and Dwight Eisenhower. None won New York City's vote. The last Republican to do so was Calvin Coolidge, whose legacy was the economic bubble leading to the Depression.

Being a New Yorker was never any help in gaining the city's approval. Thomas Dewey achieved fame for bravely prosecuting local mobsters and then served ably as governor; he lost the city's vote to Missouri's Harry Truman. Dwight Eisenhower led the Allied forces to victory in 1945 and then became president of Columbia University on Manhattan's Upper West Side (though some say that this was a mistake, and that the *illustrissimi* of the university had meant to dial up his brother Milton instead); after going on sabbatical, he was drafted to run for the White House, but New Yorkers voted for Adlai Stevenson of Illinois. When Nixon returned from Washington, he failed to persuade even the board of an apartment building to approve his residency. He subsequently moved (kiss of death!) to New Jersey.

How the Republicans found themselves in this wretched state dates back to the party's founding 150 years ago, and reflects its virtues at least as much as its failures. The party was started with vital backing from a number of New Yorkers, including Horace Greeley, the editor of the *Tribune*; its creed was anti-slavery, and the city's Republicans provided the crucial platform in 1860 for Abraham Lincoln's famous speech at Cooper Union. “Let us have faith that right makes might,” intoned Lincoln, in words that would capture the heart of the nation. But not New York, at least back then. In the election that followed, Lincoln was trounced in the city by a Democratic opponent, Stephen Douglas, who championed

a more nuanced approach to slavery that let states set moral standards of their own. In 1863, the Emancipation Proclamation was put into effect, declaring that “all persons held as slaves are, and henceforward shall be free.” The signatories were Lincoln and his secretary of state, William Seward, a New York Republican. New Yorkers were not impressed by this, nor by a forced draft, and riots ensued.

For much of the 19th and 20th centuries the city's local politics were dominated by Tammany Hall, as the local Democratic organisation was known, which provided modest services for the poor in exchange for votes and at the cost of massive corruption. Typically, when Republican mayors have managed to come to power, it has been because their independence provides them with some credibility in promising reform and taming big government. This has been the case with both the current mayor, Michael Bloomberg, and his predecessor Rudolph Giuliani (both former Democrats). The problem with independence, however, is that it does not lead to a large, enduring organisation. Neither man created a machine to register new voters and support new candidates, let alone hand out patronage jobs. Mr Giuliani has gone on to defend in public the foreign policy of the Bush administration. Anywhere else, local Republican support for a Republican president would seem to be inevitable. In New York, it has been front-page news.

Rockefeller's legacy

If independence has done little to build a large vibrant party, playing to the crowd has proved to be even worse for both the city and the party. In the 1960s, Mayor John Lindsay and Governor Nelson Rockefeller drew Democratic votes by loving big government as much as any Democrat. Their legacies include massive construction programmes for housing, highways and higher education; huge pension obligations to public employees; the highest minimum wage in the country; vast entitlement programmes; and an extraordinarily sophisticated approach to municipal finance through a Byzantine network of semi-autonomous agencies that allows the surreptitious issuance of ever more debt. After their spells in power, both city and state had become financial basket-cases. Ruinously high taxes undermined the solvency of businesses. Jobs disappeared. Growth expired. Worse still, Republicanism ceased to be ideologically distinctive. Not surprisingly, both men are remembered fondly by many Democrats.

Given the sorry record, many think it is a huge mistake for the Republicans to have chosen New York for their convention. This, however, ignores how much politics has become a business of expectations. If John Kerry got little bounce from having his convention in Boston, it is because he had long since been crowned a local prince. There was no bounce to get. In Mr Bush's case, expectations are so low that they can only be exceeded. If the president finds one New Yorker who, unable to catch a ride out of town, discovers that Republicans are not only human, but likeable, it will be one more vote than history would suggest he could get. If he does not, he can console himself that even his most illustrious predecessors did no better.

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Venezuela

Twice bitten, thrice lucky

Aug 19th 2004 | CARACAS
From The Economist print edition

AP

After declaring victory in a mid-term recall referendum, President Hugo Chávez rules the roost

Get article background

IN A supreme irony, the referendum Venezuela's opposition had been demanding for almost two years looks likely to end up gluing the country's populist president, Hugo Chávez, more firmly than ever to the presidential chair. On August 16th, the pro-government majority on the electoral council (CNE) announced that the president had an unassailable lead of 58% over 42% for the opposition. Despite protests by the CNE's two minority members, and the claim by the leaders of Democratic Co-ordinator (CD)—the broad opposition alliance—that a “gigantic fraud” had been perpetrated, international observers endorsed the result.

The announcement of Mr Chávez's victory was a shock to his opponents. After spending an average of nine hours in line due to the high turnout, they had gone to bed comforted by exit polls indicating that they had cast enough votes to get rid of the president. They awoke to the news that more of their compatriots had voted to save the man. In spite of their protests, international observers, led by Jimmy Carter, a former American president, and César Gaviria, the secretary-general of the Organisation of American States (OAS), were quick to endorse it as fraud-free. Foreign governments—including, albeit somewhat reluctantly, the United States—swiftly recognised the result.

As so often before, the principal CD leaders dithered. Though harder-line elements sought to organise street protests, most opposition voters seemed more inclined to lynch their own leaders than engage in what appeared to be a futile effort to overturn the result. On August 17th, however, international observers announced that there would be an audit of the vote, following opposition allegations that the electronic voting machines, used for the first time in the referendum and supplied by a consortium with links to the government, were tampered with. If fraud is uncovered, the referendum could be invalidated. But if Mr Chávez's victory is confirmed, the CD faces disintegration.

This is the third time in just over two years that opposition efforts to oust Mr Chávez have left the former army officer stronger than before. A series of national strikes that began in 2001, followed in 2002 by a short-lived coup and a strike that paralysed the oil industry, all failed to shift him. Instead, he used the coup and the strike as an opportunity to purge the armed forces and the state oil corporation, Petróleos de Venezuela. This left him in undisputed control of both institutions.

Obliged to take another approach, and despite its misgivings about Mr Chávez's respect for democracy, the CD then decided to take advantage of the recall referendum provided for in the 1999 constitution. Its attempts to gather the required 2.4m signatures, however, were repeatedly stymied by the CNE, whose pro-government majority seemed determined to avoid the referendum.

By the time it was finally scheduled, the government had, it now appears, bought enough time to consolidate popular support. A massive increase in public spending, thanks to high oil prices, together with a rapid expansion of emergency welfare programmes and the blatant diversion of public funds for political purposes, seem to have won the day. The opposition's feeble and unimaginative campaign was no match for government propaganda.

Mr Chávez has now announced a “new stage” of what he calls his “Bolivarian Revolution” (after the independence hero, Simón Bolívar), a blend of nationalism and populism. The electoral patrols—neighbourhood groups which successfully turned out the pro-Chávez vote—are to be maintained, and their role extended. Legislation that will further encroach on already endangered civil rights, including bills on the media and the police, is in the pipeline. Elections next month for mayors and state governors could well extend the government's power over the regions and further weaken the already groggy opposition. In response to the recall referendum aimed at the president, the government's supporters collected signatures for similar recall ballots against opposition legislators. These could well restore a comfortable pro-Chávez majority in parliament.

Having tried all the options short of guerrilla warfare, the anti-Chávez forces in Venezuela are faced with some difficult choices. If the referendum results are upheld but they persist with the claim of fraud, it makes little sense for them to participate in future elections. Not to do so, however, will merely hand the government an easy victory. Armed opposition, already planned by some groups on the right, may garner more support. But so long as oil prices remain high, Latin America's most successful populist since Juan Perón may be invulnerable.

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The Dominican Republic

Sweat and tears

Aug 19th 2004 | SANTO DOMINGO
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Can the new president turn around a tottering economy?

PEOPLE in the Dominican Republic have very little to be happy about. As the country's new president, Leonel Fernández, himself pointed out in his inaugural speech on August 16th, the country has seldom been in such bad economic shape. Yet Dominicans welcomed Mr Fernández with fanfare. An enormous sound system was deployed along the palm-lined seaside promenade of Santo Domingo, the capital, and the *merengue* beat blared out into the small hours. The party may be short-lived, however. To address his country's woes, Mr Fernández is offering a lot of Churchillian belt-tightening and self-sacrifice. This will probably mean sweat and tears, but hopefully no blood.

Until 2001, the Dominican Republic was one of the region's great success stories. With a vibrant tourist industry, a booming “assembly for export” sector and political stability, the country prospered. Indeed, the fact that Mr Fernández was president from 1996 to 2000—and is thus closely associated with the good years—was the major reason for his victory

Since then, however, the country has come to resemble an old-fashioned banana republic. Since last year, prices have grown by over 50%. The national currency has lost almost half its value in the past two years, and the country is now heavily indebted. There are frequent power blackouts, and poverty has increased to such an extent that many are now prepared to take Cuban-style risks to escape the island. Last week, 55 people died trying to reach the relative prosperity of nearby Puerto Rico.

Some of the problems were inevitable. The recession in the United States hit the country's export industries, and the terrorist attacks of 2001 dampened the thriving tourist sector. But they were compounded by the reckless economic mismanagement of the previous government, led by Hipólito Mejía. In 2003, about 20% of the country's GDP went into an overgenerous and otherwise questionable bailout of the country's third largest bank.

Mr Fernández's immediate priority is therefore to tidy up government finances in order to restore confidence in the economy. These are also the conditions for a vital $600m stand-by arrangement with the International Monetary Fund to be revived. To achieve that, the new government has proposed raising taxes. As part of the new era of “austerity” announced on August 16th, Mr Fernández also promised to cut spending by 20%.

Will he be able to pull this off? Bernardo Vega, a former ambassador to Washington and now a consultant, points out there is “a lot of fat” to cut in public expenditure. Under Mr Mejía, the government payroll increased by 30% to culminate at about 400,000 employees—twice as many as in the assembly sector. Furthermore, there are signs that the economy is recovering. Although the export sector remains flat, the two other drivers of the economy—tourism and remittances from America—are doing better than ever.

Mr Fernández's prospects, however, depend heavily on the opposition. Mr Mejía's Dominican Revolutionary Party still has an outright majority in the Senate and the largest block of votes in the lower Chamber of Deputies. Some legislators, disenchanted with Mr Mejía, will certainly want to work for tax reform with the new president. But others will be looking for him to fail.

The new president will have to push for reform during his first 100 days, while he is still riding high in the opinion polls. But if he stumbles in the next few months, it may be a very long slog ahead for both him and his country.

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Haiti

Football diplomacy

Aug 19th 2004 | SANTO DOMINGO
From The Economist print edition

Haitians unite—for a day

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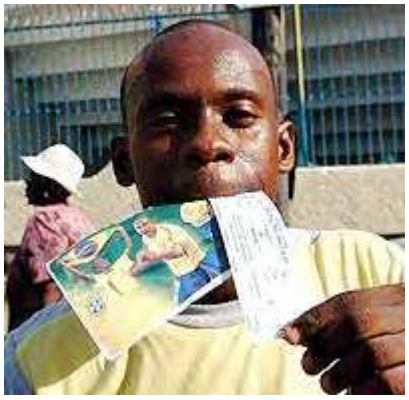
EPA



Living for football

PRINCE FELIPE of Spain and his new bride may have been in the Dominican Republic this week to acclaim the new president. But the royalty most locals were interested in were on the football pitch on the other side of Hispaniola. On August 18th the Brazilian team was in Haiti for a match against the national side in Port-au-Prince. As Brazil now constitutes the bulk of the UN stabilisation force in Haiti—keeping an uneasy peace after former President Jean-Bertrand Aristide was ousted in February—it was thought that the country's footballers, who are idolised in the impoverished Caribbean island, might help win over many hearts and minds, and—for a day—foster reconciliation.

Originally, the idea was that Haitians would swap their guns for tickets to the game, thus encouraging the general disarmament that the new transitional government of Gérard Latortue is struggling to achieve. The idea was quietly dropped when it appeared that this could be seen as a reward for carrying a weapon, and that only antiques were likely to be given up. Criminal gangs, former Aristide supporters and the rebels who pushed Mr Aristide into exile are determined to stick to their guns. In addition, football-mad Haitians were starting to manufacture home-made weapons to get a seat. So fans eventually had to buy their tickets with folding money rather than an AK-47.

Not that the Brazilians were counting on too much peace in Haiti. They stayed in a plush hotel in Santo Domingo, travelled to Haiti under heavy protection just for the game and then left immediately. The understaffed and under-equipped Haitian police have so far been unable to dent growing insecurity and crime. Foreign governments have opened their wallets—over $1 billion was promised last month to help rebuild the country over the next two years—but are less generous when it comes to their troops. Of the 6,700 peacekeepers expected of the UN mission, which took over from an American-led interim force in June, only 2,400 or so have arrived. The mission, which was supposed to include 1,622 foreign policemen, has fewer than 250 at the moment.

But all the stars—Ronaldo included—showed up for this example of what the Brazilians call “football diplomacy”. The biggest football diplomat of them all was Brazil's President Luiz Inácio Lula da Silva, who travelled with the team to Haiti to attend the match.

In wilting heat, the Brazilians trounced the Haitians 6-0. But this did not seem to bother the Haitian fans, who went on partying long after the South American stars had left.

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Sovereignty over the Arctic

Breaking the ice

Aug 19th 2004 | OTTAWA
From The Economist print edition

Everyone wants a piece of the Arctic

A LOT of people are scurrying around the normally quiet Arctic territories of Canada this month. Diamond miners are hard at work. Oil executives are applying to build a massive natural-gas pipeline south from the Mackenzie Delta. Scientists from nine countries are completing a year-long study of the melting ice-pack. Canada's prime minister, Paul Martin, made a hurried trip last week to negotiate with the premiers of the Yukon, Nunavut and Northwest Territories. To cap it all, since August 12th the Canadian armed forces have been staging the largest exercise in the Arctic that anyone can remember.

Mr Martin's dash up north had to do with provincial politics. The diamond mining, which began north-east of Yellowknife only in 1998, will soon account for 15% of the world's supply. The three premiers wanted a bigger share of their territories' new riches; at present Ottawa takes 95% of the revenue. Mr Martin has promised them a better deal.

The military exercises, on the other hand, are being driven by international politics. Though Canada claims sovereignty over the whole Arctic archipelago, the United States has never recognised this claim: it considers the Northwest Passage an international waterway.

This quarrel has come to matter more with the growing importance of the region's mineral wealth. But not all of the Arctic's value lies underground. Under the Canadian Arctic Shelf Exchange Study, a relay of scientists from Canada, America, Japan and six other countries have wintered on the ice-breaker *Amundsen*, studying the probable effects of global warming. By some estimates, the Passage will within a decade become ice-free for much of the year. It would then offer a shipping channel from Europe to Asia some 7,000 kilometres (4,350 miles) shorter than the route through the Panama Canal.

Canada is therefore keener than ever to establish the sovereignty over the Arctic that it claimed in legislation in 1895. From time to time, America chooses literally to ram home its refusal to accept this claim. In 1969 an American supertanker, *Manhattan*,crashed through the Northwest Passage without Canada's permission (though it had to ask for help from a Canadian ice-breaker). The government of

Pierre Trudeau responded by passing a law principally to proclaim a 160km-wide management zone over the Arctic waters.

The Canadians later argued that the Law of the Sea Convention gave them the right to regulate these ice-covered areas. But the United States has not signed the convention, and in 1985 sent its own ice-breaker, *Polar Sea*,through the Passage. American, British and Russian submarines have cruised merrily under the ice-pack without Canadian permission. In another rebuff to Canadian claims, a Chinese government research ship arrived unannounced at Tuktoyaktuk, east of the Mackenzie Delta, in 1999.

The spat over the Northwest Passage is not the only one in Arctic waters. The maritime boundary between Alaska and the Yukon, stretching north into the oil-rich Beaufort Sea, has never been agreed. Canada recently protested after America sold leases for the disputed zone.

Canada's lawyers say that its claim to sovereignty is well founded but could be abandoned by dereliction. Mr Martin's government is plainly not willing to let this happen. That is why it is conducting Exercise Narwhal around Pangnirtung, on Baffin Island. And just in case nobody cares or notices, a bigger military exercise is planned for 2006.

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Brazil's local elections

Confused

Aug 19th 2004 | SãO PAULO
From The Economist print edition

A mind-boggling campaign

Get article background

IF YOU know nothing about Brazilian politics, the television advertising for next October's local elections, first aired on August 17th, is likely to confuse you. If you know a little, it will confuse you even more. The free advertising, mandated by law, comes in two half-hour chunks in which candidates appear one after the other like fishmongers; another half hour is spread throughout the day. The ads rotate daily between candidates for mayor and aspiring *vereadores*, the legislators in Brazil's 5,600 municipal assemblies.

The main mayoral candidates, entitled to lots of time thanks to their parties' strength in the Brazilian Congress and to political alliances, lavish it on American-style biopics. In São Paulo, the election's biggest prize, incumbent mayor Marta Suplicy used her seven minutes and five seconds to tell voters about her "personal side", hoping to mollify those who see her as arrogant.

When it comes to touting *vereadores*, each party fights on its own, some conceding slivers of time to individual candidates, others leaving them to clamour for attention on hoardings and banners that festoon the cities. A few manage to stick out. In São Paulo, horror-film star Zé do Caixão (Coffin Joe), clad in cape and top hat, cast a curse on corrupt *vereadores*. Ex-footballer Biro-Biro linked his candidacy to the Olympic spirit.

Vereador hour is the time to spot odd alliances and Machiavellian manoeuvrings among parties positioning themselves for the 2006 national elections. The centrist Democracy Movement Party, a fractious but powerful ally of Brazil's president, Luiz Inácio Lula da Silva, is backing a left-wing rival to Mrs Suplicy, whose re-election is Lula's top priority. Roberto Freire of the Popular Socialist Party, another refractory Lula ally, endorsed Mrs Suplicy's leading rival, José Serra. Mr Freire complains that Lula is slavishly following the policies of his predecessor, Fernando Henrique Cardoso. Confusingly, Mr Serra ran for president in 2002 as Mr Cardoso's heir.

"All parties have lost their ideological edge," says Gaudêncio Torquato, a political analyst. That goes for most of the "Communist" parties. One of them has, by dint of removing the hammer and adding two circles to the traditional symbol of world revolution, turned the sickle into a smiley face.

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Japan

Another bright young hope

Aug 19th 2004 | TOKYO
From The Economist print edition

Can the youthful Katsuya Okada lead Japan's Democrats to power?

Get article background

HE INHERITED a mess and turned it into an opportunity. After taking over the Democratic Party of Japan (DPJ) in May, when his predecessor, Naoto Kan, stepped down over a pension scandal, Katsuya Okada led the party to an impressive showing in last month's upper-house elections. The ruling Liberal Democratic Party (LDP) remains in power, but no longer looks dominant. And if the 51-year-old Mr Okada can build on his good start, he might have a chance to do what previous opposition leaders could only dream about and become prime minister.

First, however, Mr Okada must keep his grip on his own party, which will hold leadership elections next month. The DPJ's interest in sticking with Mr Okada seems obvious. Because he eschews factional politics, he can work with warring DPJ clans. He is young by Japanese standards, and telegenic. He has also shown that he can deliver on election day. Still, the LDP has ruled almost continuously for the past half-century, partly because Japan's other opposition parties have self-destructed. The DPJ, which retains an awkward mix of refugees from some of those parties, must prove that it is different. “The most important thing”, Mr Okada told *The Economist* in an interview, “is that we have to work together [towards] the same goal of changing the government and gaining power.”

Fortunately for Mr Okada, the DPJ now has many first- and second-term lawmakers who agree. Unlike some of the older lags, they are more interested in winning power, while they are young enough to enjoy it, than in fighting tired factional battles. During the upper-house campaign, Mr Okada showed them that he can deliver by focusing adroitly on two winning issues—one domestic, one foreign.

Domestically, Mr Okada turned a seeming disaster over pensions into a moral victory. Mr Kan had lambasted LDP leaders for missing payments into the national pensions scheme, only to resign when he was found to be guilty of the same delinquency. The DPJ's next choice, Ichiro Ozawa, turned out to have missed payments too. Such hypocrisy and incompetence could have left the party reeling. But Mr Okada, then secretary-general, stepped in as leader and used the pensions scandal to highlight the twin themes of transparency and accountability. He contrasted the DPJ's courageous purge with the LDP's failure to disclose which of its own members had missed payments (including Junichiro Koizumi, the prime

minister, who confessed only when a weekly magazine was about to expose him). When the ruling party pressed ahead with a scheme to overhaul pension finances, Mr Okada accused it of ramming through changes without democratic debate.

The claim stuck, partly because it resonated with the DPJ's attacks on Mr Koizumi's foreign policies. In March, the prime minister's decision to send non-combat troops to Iraq earlier in the year was supported by about half the population. But Mr Okada focused on a subsequent decision, taken without a vote, to relabel the troops as part of the new UN-authorised multinational force. This force may have to engage in combat, albeit without Japan being involved. Once again, Mr Okada argued, Mr Koizumi was arrogantly bypassing the democratic process.

Mr Okada is still cagey about how much he would overhaul security policy. He thinks approval from the UN Security Council should be required for all Japanese peacekeeping missions, although he concedes that “the UN does not always work as effectively as we would like”. So long as Japan confines itself to UN-sanctioned missions, Mr Okada says, he would relax the self-imposed restrictions that limit its peacekeepers' usefulness. The DPJ is now debating whether this requires mild tweaks to the law or bigger changes to the constitution.

Although he has internal battles ahead, Mr Okada's early knack of exploiting the LDP's weak spots should be enough to persuade potential young challengers, such as Seiji Maehara (a rising star on foreign policy) and Yoshihiko Noda (a favourite among young lawmakers two years ago), to hold off. Nor do leftish members of the party's old guard have anywhere else to go. Japan's two left-wing parties, the Socialists and Communists, were devastated in lower-house elections last November, and put in another poor showing in the upper-house poll.

Mr Okada must cast a wary eye to his right, however, where Mr Ozawa heads a group from the Liberal Party, which the DPJ absorbed last summer. Although he missed his chance to succeed Mr Kan, Mr Ozawa is a proven party-wrecker. But instead of finding a proxy to challenge Mr Okada, Mr Ozawa may prefer to back him in exchange for concessions. Mr Ozawa favours deregulation and smaller government, and constitutional changes that would loosen restraints on the military.

All of this could lead to an appealing realignment inside the DPJ. Mr Ozawa may remain influential enough to keep nudging the DPJ towards reform, of both the economy and security policy. But a base of young lawmakers will want Mr Okada to go about this in a pragmatic manner. Many will urge him to stick with his formula. Look for a few chinks in the LDP armour, and strike there. Then wait for the LDP to self-destruct for a change.

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Kashmir's peace process

Over before it began

Aug 19th 2004 | DELHI
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A promised new dawn in Kashmir looks more like sunset

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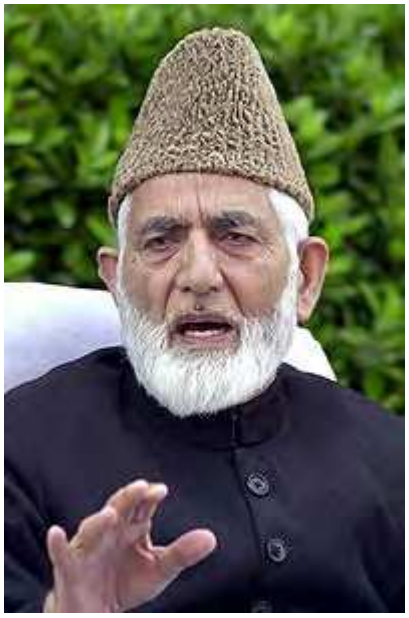

Uncompromising Geelani

RAISED hopes this year for peace in Kashmir's 15-year insurgency rest on two flimsy props. The first is an elaborate peace process between India and Pakistan, the two nuclear-armed neighbours that contest sovereignty there. The second is a parallel dialogue between the government in Delhi and moderate separatists in Indian-controlled Kashmir. The first prop has apparently survived India's change of government in May, and will next month bring direct talks between the two countries' foreign ministers. But, after just two rounds of exploratory talks before the elections, the second is crumbling, with worrying implications for the broader peace process.

A big part of the trouble is the worsening rift within the separatists' forum, the All-Party Hurriyat Conference. Always split over whether or not to talk to the Delhi government, one of its leading lights is now giving warning of “civil war”. A “unity force” set up to bring the factions back together this month dissolved itself in despair. A few days later, Syed Ali Shah Geelani, the Hurriyat's most uncompromising leader, launched a new party. Mr Geelani, who believes that in 1947 Kashmir's Muslim majority was cheated of its birthright—accession to the Islamic Republic of Pakistan—remains steadfastly opposed to talks with India.

Members of the moderate rump of the Hurriyat, led by Umar Farooq, a senior Muslim cleric, have been less concerned with pursuing talks with the new government than with trying to regain lost unity, and bolster their own support. In that, India has given them little help. Concessions they had hoped to win by taking part in talks—such as prisoner releases and a reduction in human-rights abuses by the Indian army—have not materialised. Nor has there been a breakthrough on an Indian proposal, hugely popular in Kashmir, to open a bus route across the “line of control” that divides the territory into zones of Indian and Pakistani rule.

In talking to India at all, the moderates ran the risk of reprisals by extremists, and also of undermining their own credibility and perpetuating the split in the Hurriyat. Indeed, cynical Kashmiris see these as India's aims all along. But, in the short term at least, the winner in local politics has been the pro-Pakistan, Islamist tendency represented by Mr Geelani. The losers have been the moderates and those nationalist groups that want independence from both India and Pakistan.

Violence persists, in a war that continues to claim 3,000 lives a year. India says Pakistan has reneged on its pledge to stop the infiltration of militants across the line of control. This week, the Home Ministry's annual report accused Pakistan of continuing the practice of “exporting cross-border terrorism as an instrument of state policy”. Few doubt that Pakistan is continuing to fuel the conflict. But most of the militants are young native Kashmiris.

“Kashmir's children live in a state of perpetual anger and frustration,” according to a report by Wajahat Habibullah, a senior Indian civil servant. That report, written when the author was on sabbatical at the Institute of Peace, a think-tank in Washington, DC, has stirred up a controversy in India. It suggests that America, which is regarded by Kashmiris as an “honest broker”, could facilitate a settlement to the conflict. And so it might—except that this comes close to what Indian opinion has always regarded as an

unacceptable heresy: the “internationalisation” of the Kashmir dispute.

Since Mr Habibullah is seen as close to the family of Sonia Gandhi, leader of the ruling Congress party, India's opposition Bharatiya Janata Party saw a chance to make political capital out of his subtle and balanced analysis, and labelled it “anti-India”. This does not bode well for the future of India's bipartisan consensus on the peace process with Pakistan, and hence may spell trouble for the process itself.

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India's north-east

Fraying at the edges

Aug 19th 2004 | DELHI
From The Economist print edition

Trouble beyond the chicken's neck

Get article background

IT IS not just in Kashmir that India's independence day celebrations on August 15th provoke mixed feelings. In the north-east of the country, seven states linked to the rest of India by a narrow “chicken's neck” skirting Bangladesh, secessionist movements are rife. A gruesome reminder of this was a bomb explosion in Assam on the day itself. Most of the 18 dead were school children. The United Liberation Front of Asom has claimed responsibility.

Unfortunately for the Indian government, however, ULFA is just one of dozens of militant outfits sparring with its forces across the region. Closest to outright revolt is the small state of Manipur, sandwiched between Assam and Myanmar, with a population of about 2.5m and a patchwork of ethnic rivalries. These have been set aside, in a concerted campaign against Indian rule. The spark was the death last month of a 32-year-old woman. The authorities say she was a member of the armed underground, and was shot trying to escape. Protesters, who have brought Manipur to a halt ever since, say she was raped, mutilated and murdered in army custody. This, they say, is typical of the human-rights abuses to which they have been subject for decades. At least two people have died in the protests, including a student who set himself on fire. His funeral on August 18th provoked new violent protests.

The immediate demand is for the lifting of the Armed Forces (Special Powers) Act, which gives the army in Manipur and much of the rest of the north-east sweeping powers to search, detain and shoot. The state government, which like its federal master in Delhi is a coalition led by the Congress party, has taken Imphal, the state capital, out of the act's scope. This has not satisfied protesters, but it has irritated the central government. But ministers in Delhi have not been speaking with one voice. The turmoil constitutes one of the first crises to confront the new government. So far, it has not given any sign of knowing what to do, beyond waiting and seeing. Pradeep Panjuvam, a journalist in Imphal, says people are wearying of the agitation, and its leaders are now under pressure to reach a negotiated settlement rather than watch it fizzle out. But there is enough anger to fan the flames for a while yet.

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Cambodia

The blogger king

Aug 19th 2004 | BANGKOK
From The Economist print edition

King Sihanouk announces his abdication—online

“NATION, religion, king,” runs Cambodia's official motto. For the time being, however, the country is going to have to get along without the last of the three. Norodom Sihanouk, at various times absolute ruler, prime minister, rebel leader, film-maker and, currently, constitutional monarch, left Cambodia eight months ago. He will not return, he announced earlier this month, until Cambodia's most senior Buddhist monk has given him permission to abdicate.

This is not the first time the king has threatened to throw in his ermine towel. In 1955, he actually did abdicate, in order to compete in national elections as an ordinary politician. Since he resumed the throne in 1991, after a long civil war, he has periodically tried to frighten Cambodia's feuding politicians with talk of abdication. But most threats are quickly retracted, or simply forgotten. This one, by contrast, has been vehemently repeated, most often in hand-written French notes posted on the royal website (www.norodomsihanouk.info).

AP

I've had enough :(

Hun Sen, Cambodia's increasingly autocratic prime minister, insists that the king has no right to abdicate. The constitution, at any rate, makes no mention of it. The top monk, on whom the king's fate supposedly rests, is a pal of the prime minister, so is unlikely to approve any royal retirement schemes. In the meantime, the constitution does empower the president of the National Assembly to act on the king's behalf in his absence, so laws continue to be promulgated, appointments made, and so on.

So what is the king up to? Some say he is simply old, cranky and cross at being sidelined in recent negotiations to form a new government. Another theory holds that he wants to embarrass Mr Hun Sen, who managed to get himself re-elected prime minister last month thanks to some constitutionally suspect manoeuvres. The whole kerfuffle has certainly highlighted the inadequacy of the succession laws. In theory, a special council will choose a male member of the royal family to serve as king within seven days of the current one's demise. But there is no law spelling out how the candidates will be nominated, what to do if the council is divided, or how to cope with an abdication.

According to the most radical explanation, the king really does want to abdicate, so that he can form a political party and sweep Mr Hun Sen from power. King Sihanouk may well dream of such a step, akin to his dramatic move in 1955. But, at 81, he is too old and infirm to re-enact his finest moments. His antics' failure to move Mr Hun Sen simply highlight how firmly the prime minister is now ensconced. What's more, exile is not so hard to bear. The king so enjoyed his four-month stay in North Korea that he awarded a medal to Kim Jong Il, his dictatorial host. China, where he is now, provides free medical care—and, apparently, good internet access.

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Air travel in Afghanistan

Not just for the brave

Aug 19th 2004 | KABUL
From The Economist print edition

But don't expect duty-free booze

Get article background

WHEN it first reopened after the Taliban's fall, Kabul International Airport was no place for the faint-hearted. UN planes touched down on a runway hastily patched up after cruise missiles had gouged out craters 17 metres deep. A nervous flier's nightmare of aircraft wreckage from years of war was scattered round about.

Two and a half years later the airport has changed beyond recognition, becoming one of Afghanistan's brightest symbols of reconstruction and a lifeline to the outside world. The wrecks have been carted off to the city's main scrapyard, minefields are being cleared as jets land next to them, and a passport control has been set up where arrivals once wandered in at will.

Alongside the airport's revival has come a boom in the airline business. Ariana Afghan Airlines, the national carrier that once had a terrifying reputation for crashes, now flies to 13 foreign destinations. The two aged Boeings it lost to American bombs in 2001 have been replaced by Airbuses from India, although financial problems limit the purchase of spare parts. Last year saw the launch of Afghanistan's first private airline, Kam Air, with passengers preferring its reasonable prices on domestic connections to long journeys on potholed roads menaced by bandits. Seven or eight more private airlines are planned, with romantically named outfits called Pamir, Khyber and Marco Polo hoping to get airborne soon.

The airport now sees 70-75 daily arrivals and departures, including military flights, handling around 20,000 passengers on a good week, compared with almost none three years ago. Foreign airlines landing at Kabul include Pakistan International Airlines, Iran's Qeshim Air, and soon, it is hoped, Germany's LTU. Lufthansa and Indian Airlines have reportedly sent officials to take a look. Azerbaijan Airlines flights are full of aid workers heading for a break in racy Baku.

There's still that notorious runway, however. Passengers endure a bumpy touchdown, and landing gear is sometimes damaged. There are no lights for night-time take-offs and landings, pilots find the approach over the mountains a challenge, and the quality of fuel is said to be so poor that pilots take care to bring enough for the return journey.

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Iraq

A step back from the brink

Aug 19th 2004 | BAGHDAD
From The Economist print edition

Reuters

Iraq's national conference may have persuaded the firebrand of Najaf to cool down

Get article background

THE two-week-long siege of Muqtada al-Sadr and his fighters in one of Shia Islam's holiest shrines may be coming to an end. On August 18th, in a surprise message reportedly signed by the fiery preacher himself, Mr Sadr told the National Conference, post-war Iraq's first big countrywide deliberative assembly, that he would accept its terms for peace. An aide said that Mr Sadr would leave the Imam Ali mosque, where he is holed up, and disarm his “Mahdi Army”, but only if the American and Iraqi forces surrounding him first call a truce and pull back.

The declaration may be a stalling tactic. The interim government of Iyad Allawi demanded that Mr Sadr's militia disarm immediately or face a military strike. Sporadic explosions were still audible near the shrine on August 19th. Condoleezza Rice, America's national security adviser, warned that Mr Sadr could not be trusted. However, hopes were raised that the stand-off in the town of Najaf might end relatively peacefully.

Earlier, Iraq's defence minister had ratcheted up the pressure on Mr Sadr by vowing to storm the mosque. However, Mr Allawi's allies had also offered Mr Sadr a dignified way out. The National Conference had proposed that Mr Sadr evacuate the shrine and dissolve his “Mahdi Army”.

Mr Allawi argues that militias like Mr Sadr's have no place in a modern state and so must disarm or be squashed. If Mr Sadr has indeed decided to back down, it will save Mr Allawi from having to make a ghastly choice: either to tolerate a loud challenge to his still-fragile authority, or to risk enraging Iraq's Shia majority by confronting him. Even the many Shia who detest Mr Sadr would be horrified by a battle inside a holy place.

The siege of the mosque had dominated discussions at the National Conference, which began on August 15th. On the first day, Mr Sadr's sympathisers, though a minority among the 1,100-odd delegates, managed to sway the crowd by calling for a halt to violence in the holy city.

With emotions running high, few delegates seemed willing to articulate the government's case. One woman from Najaf complained that the Sadrists were more of a threat to her city than “American cannons”, but felt so intimidated by them that she afterwards refused to disclose her name. The conference organisers quickly put forward a resolution calling on the government to avoid violence in Najaf and elsewhere, thus defusing the issue.

The next day the anti-Sadrists had their turn. Speakers declared the need to uphold the rule of law, and that Najaf's shrines were no one's personal property. They put forward a resolution demanding that the Sadrists withdraw from the holy site, and that the Mahdi Army should ditch its guns and become a political party. The Sadrists were not given a chance to reply. The organisers cut the debate short and the resolution passed with a show of hands.

Whatever the procedural deficiencies of the debate, it was probably a rough approximation of what the delegates think, and may have increased the chances that Mr Sadr will stop shooting.

The conference's main business, meanwhile, was the selection of an interim parliament with the power to overrule the government. This has proven fraught. Some delegates complained that the system was rigged to favour the half-dozen largest Saddam-era opposition parties. These same groups were ineffectual when they dominated the Governing Council, the first post-Saddam Iraqi assembly.

Rough democracy for a rough country

Nineteen of the 100 seats in the new parliament have been reserved for former Governing Council members. The other 81 were to be filled as a block: whichever coalition won a series of run-off votes was to take all 81 seats. That gave a huge advantage to the established parties, which may not be popular, but were the only ones with the resources to build a winning coalition. Unsurprisingly, they colluded to draw up a single list, and won. Mr Allawi remained aloof, but is thought to be happy with a parliament made up of parties with which he knows he can cut deals.

Fuad Masoum, a Kurdish politician who helped organise the conference, says that the pre-cooked lists were necessary to ensure that women and minorities are represented. Given Iraq's instability, he says, it is crucial that no ethnic or religious group feels left out. Independent delegates tried to challenge the system, in favour of something more competitive, but failed.

The big political struggle was thus waged in the backrooms. Delegates say that the two main Kurdish parties, both secular-leaning, faced off against the Shia Dawa party and the Supreme Council for the Islamic Revolution in Iraq. The Kurds conceded that the Shias, usually said to be 60% of the population, had a right to a majority in parliament. But they decried what they saw as an attempt to pack parliament with Islamists.

The big parties' list ultimately won by default, when its opponents withdrew, complaining of dirty tricks. Organisers stressed that the conference was never intended to be fully democratic, and was certainly no substitute for the general election scheduled for January.

But still, the throng of clerics, tribal leaders, professionals, ex-army officers, and veiled and unveiled women at the conference looked a fair cross-section of Iraq. Perhaps more important than who sits in the new parliament will be how Iraqis view it. Will they recognise it as a reasonably representative body? If so, it could help isolate the minority who have turned to violence, not just in Najaf but in rebellious Sunni Arab towns such as Fallujah. If not, it could breed more extremists.

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The Tutsis

The “Jews” of Africa

Aug 19th 2004 | BUKAVU, GOMA AND KIGALI
From The Economist print edition

Central Africa could be stumbling towards another disastrous war. To understand why, it helps to examine the Tutsis' relations with their neighbours

Get article background

BEFORE the massacre, anonymous leaflets were circulated, calling for Tutsis to be killed. Then, on the night of August 13th, armed marauders overran the Gatumba camp. With guns and machetes, they shot and chopped 160 defenceless refugees to death. The victims were wrapped in pale shrouds and buried in a rough communal grave. The massacre took place in Burundi. The government of Rwanda reacted by announcing that it might have to invade Congo. Small wonder that outsiders find central Africa's wars confusing.

It is not yet clear who carried out the pogrom. A Burundian rebel group claimed responsibility, but witnesses reported that Rwandan and Congolese gunmen also took part. The only certainty is that the victims were mostly Congolese Tutsis.

AFP

Fresh graves; fresh reasons to fight

The Great Lakes region of central Africa could be on the brink of another catastrophic war. Fighting in eastern Congo is spilling into Rwanda and Burundi, the governments of which are both threatening to send their armies into Congo to defend themselves. The worst may yet be averted. On August 16th, Kofi Annan, the UN secretary-general, called for the UN peacekeeping force in eastern Congo to be increased from 10,800 to 23,900 troops. Extra blue helmets were rushed to the Congo-Burundi border. But the world's attention is not exactly focused on central Africa. News reports dribble out, but their context is rarely understood.

For the past half-century, the Great Lakes region has seen a steady escalation of horror. In Rwanda and Burundi, Hutus have massacred Tutsis and vice versa in 1959, 1963, 1970, 1972, 1988, 1993 and 1994. In the last and worst of these blood-lettings, the Rwandan genocide, some 500,000-800,000 people were murdered in 100 days. And still the killing continued. The conflict spread into the sprawling rain forests of Congo next door, culminating in a complex war that cost at least 3m lives, and which now threatens to re-ignite.

What fuels this inferno? Many locals offer a simple explanation. “Wherever there are Tutsis, there are problems,” says a Congolese man in the eastern town of Bukavu. “Kill them all,” adds one of his

companions, only half-jokingly. It's a repulsive wish, but common. And just as students of Middle Eastern politics cannot afford to ignore the anti-Jewish views of the “Arab street”, so those who would understand central Africa must heed the chatter of the region's market places.

Who are the Tutsis? Some anthropologists argue that the label is meaningless. But everyone in Rwanda, Burundi and Congo understands it. The stereotypical Tutsi looks like Rwanda's president, Paul Kagame: tall and thin, with a long thin nose. The other cliché about Tutsis is that they live by herding cattle, whereas their squat, flat-nosed neighbours (this includes the Hutus) subsist by growing crops. In reality, the differences between the two groups are blurred, and there is plenty of intermarriage.

In the West, the Tutsis are best known as the victims of genocide. In 1994, the Hutu-dominated government of Rwanda tried to exterminate every Tutsi within its borders, and nearly succeeded. The slaughter stopped when an army of Tutsi exiles—scattered around the region by previous anti-Tutsi pogroms—overthrew the genocidal regime and took over the country. Mr Kagame, a Rwandan Tutsi raised in Uganda, was its leader.

Since then, Mr Kagame's ostensibly multi-ethnic but actually Tutsi-led government has been ruthlessly determined to prevent another genocide and to hang on to power. Besides crushing revolts within Rwanda, his men have twice invaded Congo to hunt down the Hutu *génocidaires* who fled there. They killed perhaps 200,000 killers and innocents in Congo, and sparked a terrible civil war.

Reuters

In Rwanda, the Tutsi Paul Kagame rules

All these conflicts have been, first and foremost, about power and its perks. But because insecurity makes people turn to their tribe for protection, the faultlines of war quickly become tribal. In this region, that often means the Tutsis versus the rest.

Everywhere they live, the Tutsis are a small minority. In Rwanda, where they are perhaps 15% of a population of 9m, they have been firmly in charge since 1994. The country is peaceful and visibly better run than its neighbours. The government is relatively clean, refreshingly businesslike, and beloved of foreign donors. But the surface calm disguises wild currents below. The government's line is that there are no Hutus or Tutsis, only Rwandans. Its ideologues argue that the Hutu-Tutsi divide was a creation of Rwanda's old colonial masters, the Belgians, and that a Tutsi is simply a Hutu whose ancestors owned cows. Public discussion of ethnic differences is, in effect, banned.

Rwandan Hutus can't help noticing that tall, thin people hold a lot of the top jobs, but they risk trouble if they say so. Pasteur Bizimungu, a Hutu who served as a symbolic president of Rwanda between 1994 and 2000 (while Mr Kagame, as vice-president, called the shots), was jailed for 15 years in June for allegedly inciting ethnic hatred. His real crime appears to be simply that he fell out with the regime.

In Burundi, Hutu-Tutsi relations have been improving, albeit from a wretched base. The country has roughly the same ethnic mix as Rwanda, but its Tutsi elite has run it for much of its 40-odd years of independence, keeping the majority down with flashes of exceptional brutality. A huge massacre of Hutus in Burundi in 1993 helped to convince the Hutu regime in Rwanda that the only way to ensure its own survival was to kill all Tutsis.

Burundi is still at war, but that war is less bloody than it was. Most Hutu rebels have been brought into a power-sharing government. Burundians openly discuss ethnic issues, and a South African-style truth and reconciliation commission is planned. A few hundred diehard Hutu rebels still lob explosives into the capital, but not many people were being killed until last week. That slaughter took place near the border with Congo; the Burundian government is convinced that it was the work of Hutu militias based in Congo.

The situation in Congo is the most complex. Because it is so vast and thinly populated, refugees from its crowded, violent neighbours have been thronging there for over a century. Some 5% of the 20m people in eastern Congo are now Tutsis.

In all three countries, Tutsis feel besieged. Some Tutsis liken themselves to Israelis: they may be few in number and surrounded by enemies, but they survive because they are clever and well-organised, whereas those who would annihilate them are corrupt and incompetent.

Many non-Tutsis take a less favourable view. The street talk is that Tutsis are cunning, duplicitous and bent on regional hegemony. The genocidal Hutus in Rwanda used to call them “cockroaches”. This originally referred to the speed with which Tutsi rebels struck and scuttled away, but became understood to mean that all Tutsis were vermin. The hate-mongering continues, mostly by word of mouth: a recent rumour is that willowy Rwandan women have laced their breasts with poison to kill Congolese politicians they seduce.

There is nothing inevitable about ethnic strife in central Africa

There is nothing inevitable about ethnic strife in central Africa. The seeds were sown when German and Belgian colonists first politicised the Hutu-Tutsi divide. Arriving in Rwanda and Burundi in the late 19th century, they found sophisticated warrior kingdoms, where the minority Tutsis ruled over the majority Hutus but both groups seemed to rub along well enough. The Europeans decided that the taller, skinnier Tutsis must be a separate race, superior to the Hutus. Bewhiskered anthropologists classified them as the lost descendants of Ham, Noah's errant son.

Most of this is bunk. Yet successive colonial administrations made it appear true, by favouring the Tutsis at the Hutus' expense. They made forced labourers of the Hutus, and whip-wielding overseers of the Tutsis. They even made everyone carry an ethnic identity card.

During the run-up to independence in Rwanda, the Belgians changed their minds and started to favour the Hutus instead. The then-fashionable view was that Hutus were oppressed, and therefore deserving. The Hutus took power, massacred Tutsis, and passed laws restricting the number of university places or civil-service jobs they could hold. Juvenal Habyarimana, the Hutu despot who ruled Rwanda from 1973 until 1994, convinced many Hutus that the mere fact of his being a member of the majority tribe legitimised his rule.

In Burundi, it was the other way around. A tiny clique of Tutsi officers clung to power by force, and by persuading their fellow Tutsis that if they ever let go, the Hutus would kill all Tutsis.

In the 1990s, both countries collapsed into civil war. The fighting was bitterest in Rwanda. After Mr Kagame and his fellow Tutsi exiles invaded the country in 1990, the Hutu elite started to propagate the idea that all Tutsis were fifth-columnists. “Hate” radio and newspapers portrayed the Tutsi rebels as demonic creatures with tails and glowing eyes. The Hutu masses were carefully softened up for a genocide in which every able-bodied one of them was expected to wield a machete.

The spark came in April 1994, when President Habyarimana was murdered by unknown assassins. Within hours, Hutu militiamen and soldiers began butchering Tutsis. Those ethnic identity cards told them whom to kill. The genocide ended when Mr Kagame's Tutsi rebels won control of Rwanda, driving the killers and a fifth of the remaining population into Congo, or Zaire as it was then called.

Tutsis topple a tyrant

Hidden among the refugees, and gorging on western food aid, the *génocidaires* regrouped in Congo. So, in 1996, Rwanda's new Tutsi army followed them in. The army of Congo's dying dictator, Mobutu Sese Seko, melted before them. Mr Kagame decided that he might as well conquer the whole country. He dressed up the invasion as an indigenous revolt, and installed at its helm an obscure, greedy and thuggish guerrilla boss, Laurent Kabila.

Because Mobutu was a pink-champagne-swilling kleptocrat, most people were glad to see him go. The crowds in Kinshasa waved palm fronds to welcome the victorious Mr Kabila. The western media were largely fooled, too.

AP

It is now clear that Mr Kabila played only a minor role in his own revolt. General James Kabarebe, the Rwandan army chief in Congo at the time, told *The Economist* that across half of Congo, the rebellion involved “no Congolese soldiers. The actual fighting was all done by Rwandans.” Only once, says General Kabarebe, did Mr Kabila offer him tactical advice. “He told me: ‘Kijana [young man], tell one of your soldiers to climb a tall tree here, and another to climb a tall tree there, and let more soldiers climb more trees roundabout, then, at the command, let them all fire in the air. Your enemies will be terrified, and they will run.’”

Most of the time, Mr Kabila remained several hundred miles behind the front line, collecting diamonds and sycophants. On entering the mining town of Mbuji-Mayi, he was presented with a fat parcel of diamonds, according to General Kabarebe. At night, his bodyguards heard him chuckling himself to sleep, the rocks stashed carefully under his pillow.

Once he was president of Congo, Mr Kabila decided he no longer wanted to take orders from the Rwandans. In 1998, he threw out his Rwandan advisers. Rwanda responded by sponsoring another rebellion fronted by Congolese Tutsis.

Mr Kabila called on the people of Congo to defend his regime, but he could not cite any positive reasons why they should. He was just as corrupt as Mobutu, but without the old monster's charm. So he appealed instead to the nastiest strain of Congolese nationalism. He orchestrated a pogrom of Tutsis. His *chef de cabinet*, Yerodia Ndombasi, called them "scum, germs that must be methodically eradicated," and urged people to kill them with machetes, axes, arrows, barbed wire and sticks. Thousands of Congolese youths answered the call-up.

And a Hutu ex-president faces jail

In the end, however, Mr Kabila's bulging hide was saved by the timely intervention of Angola and Zimbabwe. Robert Mugabe, Zimbabwe's president, said he was sending his army to Congo to stop the Tutsis from carving out an empire. He also had his eye on Congo's diamond mines, but his claim to be standing up to Tutsi imperialism gives a clue as to how far the anti-Tutsi ideology had spread.

The war lasted five years and left an area two-thirds the size of western Europe a smoking wreck. In 2003, when the belligerents were too exhausted to fight on, they signed a peace deal. Mr Kabila was unable to join the celebrations, having been assassinated in 2001. His son Joseph heads a transitional government, which includes all the main rebel groups. The transitional regime is now under immense strain.

One vice-president, Azarias Ruberwa, a Tutsi who used to fight for Rwanda, is making thinly-veiled threats to pull out of the government and go back to war. This week, he flew into the eastern town of Goma, a stronghold of his dormant rebel movement. He said he was there to mourn the massacre in Gatumba. His spokesmen suggest that if the government cannot protect Tutsis, it is up to the Tutsis to protect themselves.

They can expect backing from Rwanda, which has continued to arm and supply diehard Tutsi rebels in eastern Congo, though it denies it. Rwandan troops have also made sporadic incursions across the border. In March, UN officers found weapons dropped mysteriously in the waters of Lake Kivu, close to the Rwandan border, and marked with bamboo poles.

In June, two dissident Tutsi commanders attacked the town of Bukavu, and briefly captured it. The Congolese garrison responded with some random killings of Tutsi civilians. At one point, soldiers broke into a hospital, dragged out a Tutsi patient and beat him to death with bricks. And when a pro-government militia took your correspondent hostage along with a Rwandan journalist, they tapped a grenade against the terrified Tutsi's head and gloated: “Tonight we will eat your liver.”

President Kabila has sent 13,000 fresh troops to eastern Congo to crush the Tutsi rebels. They lurk somewhere in the bush, unpaid and restless. A showdown is expected around Goma.

Wanderers and settlers

People in the Great Lakes region sometimes speak of “the Tutsi question”, an eerie evocation of Adolf Hitler's “*Judenfrage*”, but one that also obscures the bitter divisions among Tutsis themselves.

In Rwanda, the main division is between the exiles, who marched back with Mr Kagame and took over in 1994, and those who were in Rwanda at the time of the genocide but somehow survived. The *génocidaires* tried especially hard to exterminate the Tutsi intelligentsia, so it is perhaps inevitable that many of those in positions of power today are former exiles.

The genocide survivors complain, albeit quietly, that the government neglects them—the very people in whose name it rules. Because the government is so intolerant of dissent, some have been forced to flee the country. In one bizarre instance, an exiled group of Tutsi genocide survivors joined some of the heirs of the genocidal “Hutu power” movement and forged a “blood pact” against Mr Kagame's regime.

But discontent among Rwandan Tutsis is usually trumped by tribal solidarity. Although no one in Rwanda is supposed to speak of Hutus and Tutsis, they know that 85% of their compatriots are Hutu. “They would finish us off,” says one Tutsi. No Hutu would dare make such a threat in public, of course.

In Congo, Tutsis are divided between those who want to live in peace with other Congolese, and those who calculate that collaborating with the Rwandans will make them rich and powerful. The first group is infuriated by Rwanda's meddling. Enoch Ruberangabo, for example, a Congolese Tutsi deputy in the national parliament, complains that Mr Kagame's regime has deliberately aggravated the ethnic divide in Congo, and that it is Congolese Tutsis who suffer the consequences. Mr Ruberangabo's family has been in Congo since the 19th century, but yowling mobs in Kinshasa have made it clear that he is not welcome. He has ignored them. “Where do you want me to go?” he asks, “This is my home.”

Many Congolese would disagree. Researchers associated with New York State University asked a broad sample whether they thought Tutsis were Congolese. Over 80% said “no”. Some quote a Swahili saying: “Even if a log lies in a river for 100 years, it doesn't become a crocodile.”

Successive Congolese governments have treated Tutsis with suspicion. Mobutu passed a law granting them citizenship in 1972, only to revoke it nine years later. This year, Congo's (unelected) parliament is due to consider a new draft law on nationality, which might be more inclusive. But then again, it might not.

Congo's first proper election is due next year, but few Congolese believe that it will actually be held. There have been two apparent coup attempts this year, and on July 13th, eight MPs thought to be linked to Rwanda quit their posts, complaining that the government had achieved little.

The future for the Tutsis looks precarious

The future for the Tutsis looks precarious. Last week's massacre could provide a pretext for all the powers in the Great Lakes region to behave worse. The Rwandan government can cite the graves of Gatumba as proof that Congolese Tutsis need its forceful protection. Tutsi powerbrokers in Burundi may use the massacre as an excuse to hold up the peace process there. And Mr Ruberwa and his Congolese Tutsi followers may decide to take up arms again. That would be as foolish as it would be tragic. A new war in Congo would pit the Tutsis against everyone else.

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Former Soviet war zones

The hazards of a long, hard freeze

Aug 19th 2004 | STEPANAKERT, SUKHUMI, TIRASPOL AND TSKHINVALI
From The Economist print edition

AP

Unresolved wars have poisoned the newly independent republics of the former Soviet south—and could flare anew

IF THE so-called frozen conflicts of the Black Sea region are ever thawed out, somebody will need to be standing by with a very large bucket indeed.

To outsiders, that may seem like an odd warning: unless you have a special interest in the obscure enclaves of small, impoverished states, where local feuds have flared up and died down, a frozen conflict may sound like a conflict you can forget. But such a conclusion would be wrong: the region's unresolved wars—in Transdniestria, Abkhazia, South Ossetia and Nagorno-Karabakh—are a big reason why the newly independent states of the former Soviet south have failed miserably to fulfil their potential. Instead of enjoying their freedom, they have emerged into the world as stunted, embittered and ill-governed creatures. And if real fighting flares again—a process which has begun in South Ossetia (see article)—things could become far worse.

At the heart of each conflict is a claimed mini-state whose rulers prevailed, by dint of Russian arms, in a local war. While there are huge differences, these statelets have things in common. Ten years or more of isolation under unrecognised governments have left them as harsh, militarised societies, with few functioning institutions, and economies open to crime.

South Ossetia is the pettiest, but currently the hottest of the conflict zones. It is a landlocked province of Georgia which would have no viability as a legitimate country. It survives as a conduit for smuggling between Georgia and Russia, mainly in cheap spirits, arms and grain, under the diplomatic protection of the Russian government and the military protection of Russian troops.

Of the four statelets, Karabakh comes closest to being a normal society—at least for the ethnic Armenians who remain there. Nearly a million people from both sides of the war were put to flight by the fighting which concluded in 1994 with a big victory by soldiers from Karabakh and Armenia itself.

Especially since 2001, when a local bully and racketeer, Samvel Babayan, was put in jail, Karabakh—which calls itself independent but is in practice virtually joined to Armenia—has had something recognisable as local politics and a mixed economy. Investment from the Armenian diaspora has boosted

the economy. One new arrival from America, Vartkes Anivian, started a dairy-products company after the war, and now employs 250 people. Municipal elections have just been held in the enclave—to the fury of Azerbaijan, to which Karabakh legally belongs—and there was genuine competition between the candidates. The atmosphere in Stepanakert, Karabakh's capital, is orderly in a post-Soviet way, not chaotic.

So Karabakh might have a decent future if the enclave's future could somehow be settled. Four years ago, a compromise seemed within reach: most of Karabakh would have been joined to Armenia, while the Azeris recovered the surrounding areas and gained a corridor between their republic's two parts. More recently, the mood on both sides has hardened, and a big body of Azerbaijani opinion longs to recover the land by force.

Small wars, or medium?

The fighting over Karabakh was and could again become a fair-sized war; South Ossetia by comparison is a small, though strategically significant, squabble. Abkhazia, in Georgia, and Transdniestria, in Moldova, fall somewhere in between.

Both Abkhazia and Transdniestria can make claims to special political status, if not to independence, on historical grounds. Both regimes control territories and economies capable of standing alone. But both are willing hostages of Russia, which helped them fight their wars of secession when the Soviet Union collapsed, and has given them military and diplomatic support ever since. It has issued passports so freely that probably a majority of the population in each enclave could claim Russian nationality. But Russia's "protection" has also become the main obstacle to a constitutional settlement. Russia prefers to keep the enclaves as its own pawns. At its most mischievous, the Kremlin's strategy may view Transdniestria as a second version of Kaliningrad, the Russian enclave near Poland—in other words, a trouble-making outpost on the borders of NATO. And some of the worst features of Russia's own governance have been transferred to its protégés in Georgia and Moldova: organised crime, corruption, and authoritarian leadership.

For the people of these non-countries, life goes on, after a fashion. "It is a normal town, but blown up a bit," says a United Nations official trying to put the best face on Sukhumi, "capital" of Abkhazia. And there is indeed the ghost of something lovely in the landscape, where the beaches curve north to the Russian border.

"It is a normal town, but blown up a bit"

But to call Sukhumi "normal", even by the elastic standards of the Caucasus, is stretching things. For one thing, half of its population is missing. Ethnic Georgians fled the city or were driven out in the civil war of 1992-93. And to say that Sukhumi is blown up "a bit" risks flattering a town where only about one-third of the buildings are in good shape, one-third are badly run down, and one-third are derelict. The roads are crumbling, the pavements are grassing over, and the airport is dead save for a few UN helicopters. Tourists from Russia are the mainstay, along with agriculture, of the

visible economy. The invisible economy belongs to burly men who drive smart cars with handguns on their hips. They, or their like, run a blacker-than-black trade centred on the port. Smuggling probably involves drugs, arms, fuel and stolen cars. “Whatever you have”, says the UN official, “it disappears into a black hole when it hits the docks.”

Tiraspol, the capital of Transdniestria, presents a more orderly façade. Streets are eerily quiet and clean, and almost bare of cars, even on a weekday afternoon. Nobody in civilian clothes carries a gun openly. A statue of Lenin looks down from a pink marble column in front of the presidential palace. The Bolshevik leader looks uncannily like Transdniestria's own bearded “president”, Igor Smirnov, a former metalworker from Kamchatka in the Russian Pacific who moved to Tiraspol in 1987 as a factory manager and manoeuvred his way into power. Mr Smirnov's son heads the “state customs committee”, the second-biggest job in a land which lives largely on trade, licit and illicit, between Ukraine and the rest of Moldova.

In the past month both Moldova and Ukraine have announced much tighter customs controls on goods moving out of Transdniestria. Moldova was retaliating against a decision by the authorities in Transdniestra to shut schools there still teaching Romanian in the Latin alphabet.

But despite such occasional flurries of firm government, experience suggests that Transdniestria's borders will remain porous enough for it to go on supplying Moldovan markets with untaxed consumer goods, and to go on shipping its more sinister cargoes, including arms, out through Ukraine or by air. According to a recent report from the International Crisis Group, a Brussels think-tank, Transdniestria has five or six arms factories making small arms, mortars and missile-launchers, for sale to the world's trouble-spots. A recent study from the German Marshall Fund of the United States has called the conflict zones “unresolved fragments of Soviet Empire [which] now serve as shipping points for weapons, narcotics, and victims of human trafficking, as breeding grounds for transnational organised crime, and last but not least, for terrorism”. That may be a bit too hard on Karabakh, but a fairly accurate account of Abkhazia, South Ossetia and Transdniestria. It may be time for the world to slop them out.

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South Ossetia

We don't want war, but...

Aug 19th 2004 | EREDVI, GEORGIA
From The Economist print edition

Resolve and regret in a reluctant war zone

AS EXPLOSIONS from rocket-propelled grenades flashed and thudded on the outskirts, the defenders of this village, who happen to be on the Georgian side of South Ossetia's incipient conflict, seemed resolved but hardly gung-ho. “To be shooting at each other in the 21st century—it's crazy,” mused Guram Vakhtangashvili, a local politician. Compared with many brewing conflicts, the parties to this odd little war have little stomach for a fight—in part because they know each other well.

An agreement on August 17th to cease fire and remove unauthorised troops offered some hope, but it was the second truce in four days and in Eredvi there was little optimism. That very day, at least three Georgian soldiers were killed in this breakaway province where Tbilisi wants to reassert control.

Surrounded by orchards, maize fields, vineyards and the rolling foothills of the Caucasus, Eredvi's 5,000 people might in better times be envied. But a tall, forested hill dominates Eredvi and it is from there that Ossetian forces have lobbed mortar shells around and occasionally into the settlement. On both sides of this intimate war, farmers, teachers and policemen don camouflage to help regular troops stand guard or fight. And as soon as 1,000 Georgian children were evacuated last weekend, most mothers returned to support their men.

In Eredvi, few blame ordinary Ossetians. Fury is aimed at the Ossetian leader, Edward Kokoity, and at Russia, which Georgia accuses of arming and training Ossetian guerrillas.

Among Ossetians, similar loathing is directed at the Georgian state. They have raw memories of the 1991-92 war, in which Georgians behaved badly. In a churchyard in Tskhinvali, the local capital, women prepare a stodgy dish of *plov* for their men, on the front-line, and rail against their foes. “The Georgian authorities provoke us—they want this place, but they've never owned this land and they never will,” declares one.

In reality, boundaries between the communities blur, and many families are mixed. “It's a problem,” said Ilya, a Georgian policeman, gesturing at an Ossetian checkpoint 200 metres from his own. “I know the police there. I never fire on them because they're friends—and they won't fire either.”

Because there is no electricity in Eredvi, the starlight is brilliant. But for a local man who shares a balconied, vine-covered house with his mother, nights mean danger and duty. He is bitter—about the Russians, the Ossetian leaders, and even about Mikhail Saakashvili, “a temperamental president”. But, he says softly, “Retreating is out of the question. My mother and I will stay here—and this is where we will die.”

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The European Commission

A leap forward, or a long march

Aug 19th 2004 | BRUSSELS
From The Economist print edition

The new Eurocrats are market-minded folk—but not everything suits Britain

WHEN the bureaucrats of a newly enlarged European Union jerk back into action after the torpor of summer, will they be able to inject some new zest into an enterprise which—to the rest of the world, anyway—looks tired and over-stretched?

Or to put the question another way, will an erstwhile Maoist who is now a market-minded reformer be the man to achieve Europe's long-awaited Great Leap Forward? The first signals sent by José Manuel Barroso—the Portuguese politician who will shortly take over the European Commission—seem encouraging for those who see deregulation and freer markets as the way to reinvigorate Europe.

Last week, he named a new commission in which four of the key economic posts—trade, competition, internal market and agriculture—went to card-carrying liberal reformers. People at the other end of the spectrum are nervous already. The outgoing French trade commissioner, Pascal Lamy, says the Union's policies could now be “more liberal, more Atlanticist”.

Worse still from his viewpoint, Mr Lamy believes the new trade commissioner, Britain's Peter Mandelson, could try to resurrect a free-trade zone with the United States—the so-called Transatlantic Market Place, which is backed by Britain's economic policy-makers, and hated by the French establishment in equal measure.

Tony Blair has already expressed his satisfaction with the Barroso team and their free-market credentials. The former Portuguese prime minister has also pleased Britain by pledging to make the EU's so-called Lisbon agenda of economic reform and modernisation a priority.

So much for the tactical British victory, which has also been underlined by the appointment to a top commission job of Ireland's tough ex-finance minister, Charlie McCreevy. But has there really been a setback for what might be called the “old European” axis of France and Germany?

In Berlin, Chancellor Gerhard Schröder has been full of smiles over the naming of his fellow Social Democrat, Günter Verheugen, as commissioner for enterprise and industry; and the job description is the one Mr Verheugen himself said he wanted. But the appointment falls well short of Germany's ideal scenario: the naming of a “super-commissioner” for economics. Instead, Mr Verheugen will have a “co-ordinating role” among the other commissioners with an economic brief—but not the right to overrule them. Although he has been an effective promoter of the enlargement process, some see a certain irony in putting a German Social Democrat in charge of competitiveness: his home country has the third-worst record for implementing internal-market legislation—beaten only by Greece and France, a nation whose belief in European integration is not always translated into practice.

The biggest loser from last week's appointments was France. Its former employment minister, Jacques Barrot, had to settle for his second-choice commission job—the transport portfolio. Mr Barroso sweetened the deal by making Mr Barrot a “vice-president”, but the title means little.

To what extent will Mr Barrot be able to swim against the liberalising tide? Under the heading of transport there are certainly some important areas where deregulation could be held up. For example, Mr Barrot will be handling some sensitive talks on the future of transatlantic aviation. But there is still a feeling in Brussels that on Mr Barroso's watch, France will no longer enjoy the huge influence that once seemed like an automatic entitlement for a prime mover in founding the Union.

But not everything is going Britain's way: there is one perverse manner in which the Barroso commission

may embarrass the British government. While Mr Blair would prefer the commission to stay mum in the run-up to Britain's referendum on the EU's constitution, Mr Barroso has declared one of his priorities to be countering Euro-apathy—in other words, he wants more people to be told about what the Union does and why. Taken together with his pledge to put his team in Europe's “driving seat”, there is ample scope for Mr Barroso to upset those in London whose fondest wish is that the Brussels bureaucrats should neither be seen nor heard by anybody in Britain.

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The EU and competition

A real Monti?

Aug 19th 2004 | PARIS
From The Economist print edition

Neelie Kroes must work hard to match her predecessor's zeal

ONE of the surprises of the European Commission—for people who follow these things—was the fact that Neelie Kroes, a forceful Dutchwoman, was put in charge of competition, not transport.

The job is a tough one, and her predecessor, Mario Monti, is a hard act to follow. He strengthened the Union's competition department and was successful in most of his battles against cartels, state aid to sickly companies and mergers that harm competition. As the Union expanded in May, he devolved some of the oversight of EU competition rules to member states—so he could focus more on fighting what he saw as hard-core antitrust cases.

In July, Mr Monti introduced tougher rules on state aid, due to take effect in October. Most people expect Ms Kroes to show a similarly robust spirit when dealing with member states. She won her free-market spurs when she helped push through the privatisation of the Dutch post and telecoms agency.

Companies at odds with Brussels on competition rules, especially American ones, hope Ms Kroes will be more sympathetic to business than Mr Monti was. Having served on the board of several multinationals—such as Lucent, Thales and Volvo—she knows their concerns; but that does not mean she will be their patsy.

So her handling of Mr Monti's unfinished business will be an important sign of what corporate Europe can expect. The biggest pending case is Microsoft's appeal at the EU's Court of First Instance against the €497m ($613m) fine imposed by the commission in March for “bundling” new features into Microsoft's Windows operating system, to protect its near-monopoly of the personal-computer market.

Then there is another long-standing row with a big American company: Mr Monti's five-year campaign against Coca-Cola's allegedly unfair selling practices in Europe. The company says rebates and discounts are good for consumers, and the commission is penalising big firms' success.

Ms Kroes will also be confronted with the troubles of Alstom, France's sickly engineering group. The French government's latest rescue package for Alstom, approved by the commission on July 7th, is unlikely to win approval. The more you think about this daunting in-tray, the clearer it becomes why the French contender, Jacques Barrot, was not deemed the right person to wear the Monti mantle.

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Spain

When the music never stops

Aug 19th 2004
From The Economist print edition

Spain's ruling Socialists fail to call time on the patronage game

"WE THOUGHT the days of governments giving jobs to friends, meddling in companies and overriding shareholders were a thing of the past." The reasons for this outcry from Eduardo Zaplana, a slick spokesman for Spain's centre-right opposition, are obvious to anyone who has seen the sweeping personnel changes, in every area of public and semi-private life, which have followed the Socialist election victory last March.

In the finest traditions of Mediterranean democracy, heads have been rolling in every agency under the government's control—and in many places that are supposed to be independent. There have been purges at think-tanks, the judiciary and the Cervantes Institute, which represents Spain's culture. The state-owned media, several key embassies, the security services and Madrid's museums have all seen changes at the top.

It is true, of course, that every democracy plays musical chairs by its own rules. Newcomers to America are often amazed by how many jobs change hands with a new administration; in Britain, the scope for government patronage—while amply exploited—is comparatively limited. But in Spain, as in many parts of southern Europe, new administrations play patronage games with a gusto that amazes people from further north.

Like every Mediterranean country, Spain has a rich set of words and customs surrounding the practice of patronage. If you have friends in high places and use them to get a job, you are said to have an *enchufe* or literally, a plug. To show gratitude for a political favour—what in America might be called a piece of pork—you can send your helper a *jamón*, a leg of ham.

It takes more than a change of government to change a political culture. But José Luis Rodríguez Zapatero, the Socialist prime minister, may have a chance to break with the excesses of political favour-trading—if he keeps a vow to respect the independence of private firms and regulators. At least in theory, the Socialists are committed to strengthening the agencies which regulate energy, financial markets, and mergers and monopolies; none of these bodies has ever had many teeth. A start has been made with the naming of a respected figure, Manuel Conthe, as head of the Comisión Nacional del Mercado de Valores, which oversees financial markets.

What everyone wants to know now is how far the Socialists will use their influence to alter the management of newly privatised companies in which the state still has a share. Already there has been one change: a Socialist ex-minister, Luis Atienza, has been put in charge of Red Eléctrica de España, a power distribution firm of which the state owns just over a quarter.

Will there be more? Pedro Solbes, the finance minister, murmurs that he wants to see "honest, competent" people in top business jobs. Mr Zaplana, from the opposition People's Party, retorts angrily: "Presidents of companies answer to stock-holders, not the government." But that is a bit rich, coming from a man whose party used to cram big firms with its cronies.

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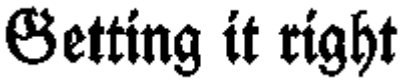
German spelling

Getting it right

Aug 19th 2004 | BERLIN
From The Economist print edition

Moves to simplify written German may have the opposite effect

WHEN Bavaria and Prussia, in 1880, introduced Spellingreform, it was a Challenge to the Rulers of newly-united Germany. Chancellor Otto von Bismarck threatened Civil servants with “increased Fines” if the new System was used. Until 1901, when the issue was finally, at a Conference of german-speaking Countries in Berlin, settled for good, there were two official Orthographies.



These days, nobody faces draconian penalties for choosing to spell differently; weaving one's way through the challenges of written German—of which the above paragraph offers a hint, for Anglophones' benefit—is considered punishment enough. But another period of division over orthography could be the outcome of a growing dispute over the latest spelling reform, introduced in August 1998 and due to become mandatory in schools in a year.

Things came to a boil when three influential publications—*Der Spiegel* magazine, the *Süddeutsche Zeitung* daily and the *Bild* tabloid—announced that they would return to the old way of spelling. Now there is talk of scrapping the reform altogether. Officials from Germany, Austria and Switzerland will hold an “emergency meeting” later this month.

Backers of reform say simplification of spelling is badly needed to make life easier for schoolchildren; rolling back now would cause chaos in the classroom and cost millions. Critics say the overhaul has failed and Germany could become a land of dyslexics.

Both sides have a point. German spelling does need overhauling: over the decades, it has grown more unwieldy. But the reform, approved by German-speaking countries in 1996, does not make the rules much easier, and in some cases the new way is harder.

Spelling can arouse strong emotions in Germany. Residents of Cologne once called the police because a coiffeur had put up a sign promoting *Haarflege* (hair care) instead of the correct *Haarpflege*. Even mighty institutions like the Bundesbank have stumbled. Having committed, in the early 1990s, the gaffe of spelling the name of a tiny island, depicted on a banknote, in the old way—an “error” invisible to the naked eye—the bank got dozens of angry letters.

What lies behind this row? With the reform, the *Länder*, Germany's constituent states, have reasserted power over linguistic standards, which had fallen to the editors of the Duden, an authoritative dictionary. Such muscle-flexing by the *Länder* has irked those who care about language, notably journalists and writers, and they are unlikely to give way. But the *Länder*, for their part, probably won't scrap the reform, if only because they would all have to agree. More likely, at the next meeting of their education ministers in October, they will opt for a German way of building consensus: creating a commission, including some writers and journalists.

Some argue that the much-lamented “spelling chaos” has some good side-effects: it has made German a more flexible language, with fewer rigid rules and more capacity to evolve. That makes it easier to learn, and less frightening.

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Exams

Incorrect answer

Aug 19th 2004
From The Economist print edition

Britain is obsessed with school exam results. Grades are rising for good reasons—but the system has some deep flaws

SCHOOL exams must do a few seemingly simple things. They should show what has been learnt, and who has done best, with grades that are both precise and meaningful. They should be rigorous, but also fair. Standards should stay steady over time, but the curriculum should be up-to-date. The courses should be accessible and attractive, yet cover all the ground that universities and employers require.

Such contradictions guarantee dissatisfaction, especially as good results in the A-levels taken in the final school years play a huge role in university admissions—and thus future earning power. So in August, which should be the quietest month in the school year, there is an annual panic about Britain's education system.

This week's A-level results showed a record pass-level of 96%, with a record 22.4 % gaining the top A grade—and prompted the usual howls of dismay about dumbing-down and lack of differentiation. A government minister, David Miliband, said the row was “a pantomime, not a discussion”. The threefold increase in students getting two passes or more over the past 30 years was a sign of improving education, he said, and those who criticised it were elitists defending “the old order”.

Yet even Mr Miliband agrees that there is a need for change in the way the best candidates are graded. Places at the top dozen universities are oversubscribed, sometimes hugely, by candidates with a plethora of A grades. It's a small problem compared with others—such as the fact that a quarter of schoolchildren never learn to read and count properly—but a politically important one.

One plan is to split the A grade into four sub-categories. Another is to publish the percentage marks scored, or to show the grade gained on each bit of the exam. Such ploys might help to distinguish brilliant candidates from the merely clever. But not necessarily: exams are only a rough measure of ability, so it may be sensible to have broad categories rather than narrow ones. Some would like an extended essay, or a new A* grade for those who answer the hardest questions. But whatever the system, the best schools will find ways of getting their candidates to do well. No system can achieve both social engineering and academic excellence.

What about the wider charge, that A-levels have become too easy? The biggest changes have been in the way that the exams work. Good exam technique matters less. Retakes are freely allowed and questions are less cryptic, with more signposting about how to answer them. The aim is to find out what candidates know, rather than what they don't. There is a great deal more coursework—with all the attendant dangers of plagiarism and cramming.

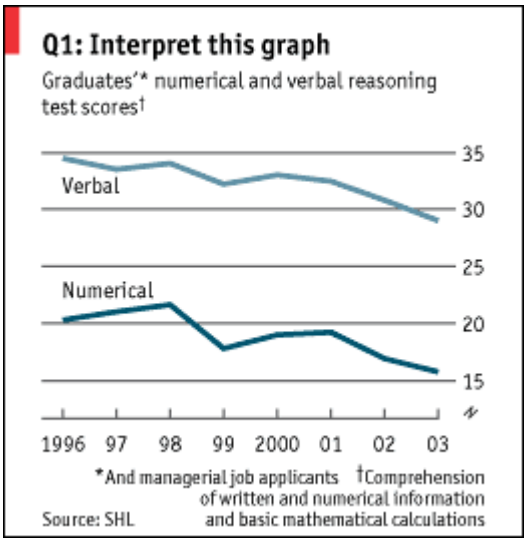
Given all that, and how much more exam-centred pupils and teachers have become, it would be odd if results did not improve. In fact, they have done so since 1982, suggesting that the trend is not a deliberate political plot. Educational results do generally improve as countries get richer. But it is also true that content has changed, and not always for the better. This is particularly true in the GCSE exams, taken at 16, which are widely seen as undemanding. But there are problems at A-level too: it's possible to get an A in maths without a solid grasp of calculus, for example. That used to be essential.

Such shortcomings certainly impose strain on the next stage in the system. A survey this week showed that 90% of academics thought A-levels had become less demanding. In the highly rated actuarial-science course at London's City University, for example, the first term of the first year is spent filling in gaps in maths that students used to learn at A-level: chiefly geometry, vectors and calculus. The university-level maths that actuaries need is crammed into two terms of the first year.

Remedial courses are widespread, but not yet very burdensome, says Universities UK, a lobby group. A-levels no longer dovetail neatly into the intensive three-year degree course that is still British universities' main offering. But it may well be better to leave universities to plug specific gaps, rather than expect all A-level candidates in, say, maths, to learn things that only a few will need. In the end, American-style levels of participation in higher education will require American-style flexibility, with more part-time degrees and greater use of credits, and a greater financial contribution from the student.

Even if the universities' complaints are largely overblown, the other big constituency—employers—is still unhappy. They once saw A-levels as a solid signal of achievement, but many now say they distrust them.

There is evidence that some basic skills are becoming patchier. SHL, the country's largest provider of private tests, has seen a steady decline in the numerical and verbal reasoning abilities of graduate-level applicants (see chart). Because there are a lot more graduates than there used to be, it is not wholly surprising that standards have dropped a bit. But there's no doubt that faith in the system is dented.



In the end, arguments about declining standards are beside the point. No exam system imaginable could provide all the information that A-levels are supposed to signal. Some sensible tweaks are possible: more differentiation of the very brightest, extra marks for good grammar and spelling in essays, a larger core curriculum in maths, fewer resits and less coursework, and less narrow specialisation. But in the end, the best exam system will be one that matters less than the education it seeks to measure, not more.

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Motorbikes

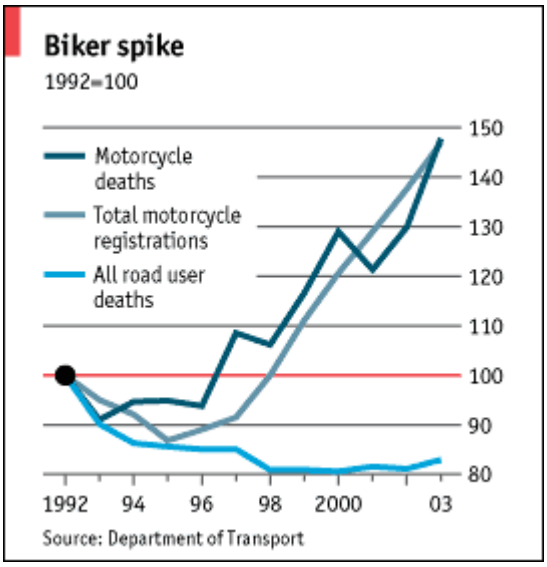
Free riders

Aug 19th 2004
From The Economist print edition

Four wheels bad, two wheels good

WHEN you buy a motorbike, the brochures promise sun, adventure and the joy of the open road. Shivering through a winter downpour in Putney isn't mentioned, but despite Britain's cold, wet climate, motorised two-wheelers are proving more and more popular.

The number on the road has grown every year since 1995 (see chart), and the market was worth £707m ($1.3 billion) in 2003, according to Mintel, a market research firm. The government reckons there are about 1.5m bikes on the road, up by half since 1998.



In contrast to other European countries, British bikers have traditionally gone for the sort of ultra-fast machines used in professional racing, says Jeff Stone of the British Motorcyclists' Federation. These are mostly owned by rich, middle-aged men who buy them for the fun factor, zooming through the countryside in search of thrills and lost youth. “It's not an everyday transport thing,” he says. “It's something to have in the garage for weekends, like a jet-ski.” But although they remain the most common type of motorbike on the road, sports bikes are not attracting many new riders: their share of new registrations has fallen by 32% since 1999.

Most of the growth has instead come from young people, who are being uncharacteristically boring and practical: they buy small-engined, European-style scooters: cheap, easy to park and good at puttering through the clotted traffic of modern British cities. “They treat them like domestic appliances,” says Mr Stone. While sports bikes have lost their allure, scooter registrations have grown, and this is expected to continue. Claire Hatcher, an analyst at Mintel, points out that besuited professional types are buying them for commuting. Ken Livingstone's recent announcement of a planned extension to London's congestion-charging scheme—which two-wheelers are exempt from—will also boost sales; motorbike traffic in the capital has risen by 15% since the scheme was introduced last year.

There is a downside. Motorbikes deserve their reputation for danger. Although accidents per kilometre have been dropping slowly, the number of deaths has climbed in step with the number of bikes, which remain by far the most dangerous way of getting around. They make up 1% of the vehicles on British roads but account for 18% of deaths and serious injuries. A recent government report made a number of sensible suggestions, including fitting new braking technology, but enthusiasts tend to resent this sort of official interference. Less realistically, the government also wants bike magazines to stop glamorising speed and giving tips about straight, empty country roads. Others suggest a tiered licensing system, already used in Japan, which would prevent new riders qualifying and then jumping straight on to fire-breathing racing machines.

Two things kill bikers: car drivers in towns, who don't notice them crossing junctions, and the bikers themselves, when they fly off bends on country roads. The government is tackling the first problem with a scheme called BikeSafe, which teaches defensive riding. As for the second, the manufacturers, after public criticism, have agreed to limit the maximum speed of the machines they produce. This might do more good if the limit wasn't set at a sizzling 300kph (186mph).

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Tourism

Don't mention the war

Aug 19th 2004
From The Economist print edition

Overpriced, and rude too? That was last year

GRAHAM GREENE once mocked the friendliness a customer receives in an American bank, where the teller “conveys a sense that he happens to be there accidentally and he is overjoyed at the lucky chance of the encounter”. Now the London Development Agency wants to import such American standards, with a £3.5m ($6.4m) four-year programme to polish hotel and restaurant staff behaviour.

European cities have long tried to shed their surly image. The annual *Bienvenue en France* campaign urges cabbies there to be friendlier to visitors. In May Russia ordered its cheerless border guards to smile. That is at least better than the campaign run by Aeroflot, the state airline, in the early capitalist years, which justified its snarling service with the slogan: “We don't smile because we are serious about making you happy.”

The development agency says the plan is not about image, but a real improvement in service standards, particularly for the business visitors who spend one tourism dollar in three in the capital. Training will include the proper way to carve meat, serve cigars and pour champagne, as well as improving the level of spoken English, and the way complaints are dealt with.

Businesses, who will pay for part of it, generally welcome the initiative. Even well-run outfits suffer when a slopped drink or rude remark in another establishment damages London's reputation.

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Northern Ireland

Warmongers, stand easy

Aug 19th 2004
From The Economist print edition

What do you do when there's neither jaw-jaw nor war-war?

Get article background

IT USED to be Europe's worst terrorist conflict. Now Northern Ireland's peace process is stagnant, yet a return to violence is not in sight. So how do politicians spend their time? Gerry Adams, the leader of Sinn Fein, is busy writing memoirs: life in the modest streets of Catholic west Belfast, occasionally fictionalised and with some immodest use of recycled speeches. There is no mention of his years at the top of the IRA—an organisation that he now hints should be disbanded.

His fellow republican Martin McGuinness used to be the IRA's chief of staff. Now he looks forward to the day when it devotes itself solely to tending graves. He once had literary ambitions too, producing a much-mocked sonnet on a sunset seen from the window of an aeroplane. But his real passion is fly-fishing. In the days of negotiations, he would regale British, American and Irish officials and politicians with stories about sea trout. Now he has more time to catch them.

The best-known republican writer is Danny Morrison. He once urged the rank and file to drive the British out of Ireland with the “Armalite and the ballot-box”. Now his weapon is the pen. Critics saw little talent in Mr Morrison's string of overwrought novels and a lurid jail diary. Journalism has proved more successful.

On the other side of the divide, Ian Paisley, the leader of the hard-line Democratic Unionist Party (DUP), has no discernible leisure interests apart from hell and damnation. His party has gone from fire-breathing outsider to the main representative of the province's Unionist majority. It's exchanging papers with the British government about negotiations next month on restoring devolved government. Since that would mean breaching the DUP's ban on negotiations that also involve Sinn Fein, it would be quite an advance. The DUP has an advantage over the Ulster Unionists, the mainstream party it displaced in last year's elections; it need not fear being condemned for backsliding by Mr Paisley.

It is the party's ambitious deputy leader, Peter Robinson, who really wants a deal. That would mean less time to indulge his enthusiasm for 1970s-style clothes, and his passionate interest in breeding Koi carp in heated pools in his garden.

If devolved government does return as a result of a deal among hard-liners, what will it mean for moderate politicians' leisure? Mark Durkan, the leader of the SDLP, which has been squeezed out by Sinn Fein, likes to jive. David Trimble, leader of the Ulster Unionists, has outside interests ranging from opera to second-hand bookshops, via Elvis Presley and German red wine. But both will have plenty to do if they're to halt their parties' decline.

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Terror and the courts

Double jeopardy

Aug 19th 2004
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A lot rests on the trial of eight Britons

FOLLOWING two weeks of interrogation, eight British men were charged on August 17th with conspiracy to commit murder and to create a “public nuisance” by means of explosives, chemicals or radioactive materials. One, Dhiren Bharot, was also charged with possessing reconnaissance plans of buildings in New York, New Jersey and Washington, DC.

Despite the gravity of the charges, officials strained to convey normality. David Blunkett, the home secretary, said simply: “We must now let the judicial process take its course.” The normal judicial process, that is—not the extraordinary powers to detain suspected terrorists obtained in 2001, nor the secret hearings Mr Blunkett mused about earlier this year. Normality is all to the good; but any trial will be perilous.

The charges are the most ambitious yet publicly announced in Britain or America since the terrorist attacks of September 11th 2001. So far, most men scooped up in anti-terrorism raids have been released without charge or tried for relatively unalarming offences to do with immigration and illegal fundraising.

Proving such a complex conspiracy case in court presents unusual challenges. Restrictions on reporting are likely, but otherwise the case against the eight men will resemble a normal criminal trial. Any “secret” evidence that might be supplied by foreign or domestic spooks must be shown to a jury, and may be challenged. If charges are dropped or, worse, convictions obtained but overturned, Muslims who are already suspicious of the police and criminal justice system will find their anxieties confirmed.

Yet guilty verdicts would also throw the government's anti-terrorism strategy into question. The power to detain suspected foreign terrorists without trial, granted in 2001, is a legal embarrassment that threatens to contaminate the rest of the judicial system. Last week, the Appeal Court ruled that judges could take into account evidence acquired through torture, so long as British agents did not connive in obtaining it. If alleged terrorists can be convicted in the traditional way, it's reasonable to ask why such draconian powers are needed in other cases.

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Retailing

Don't bother to cook

Aug 19th 2004
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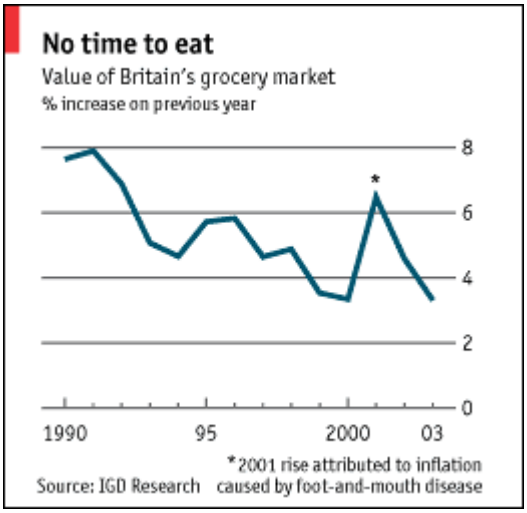
Changing palates and last-minute dining have revived the high street

Get article background

BUYING food in the high street might seem to make as little sense as grinding your own flour. For the past decade, shoppers have been going to buy their groceries (and increasingly clothes and other items) in large out-of-town supermarkets offering bargain prices. This has left many high streets drab and short of business. But now the big supermarkets are turning their attention to small stores in town centres. This week, Sainsbury's bought Jacksons, which has 114 small outlets in Yorkshire and the North Midlands, taking its count of convenience stores to around 250. Tesco will soon have four times that number.

The new strategy is partly because competition rules make taking over chains of big stores very hard. Planning laws also make it difficult for the big chains to open large new stores. Despite the occasional boon from deregulation, such as the decision this week to allow more supermarkets to set up pharmacies, growth must now come from abroad (a Tesco strong point) or from wholly new activities at home—like the new mini-stores.



Supermarkets like these for another reason: changing tastes. As Ernst Engel noted from studying statistics in 19th-century Prussia, families normally spend proportionally less on food as they get richer. That seemed to be happening in Britain, which was bad news for food retailers. But now a shift to pricier food at the top of the market is spreading downwards.

Taylor Nelson Sofres, a market research firm that measures the preferences of 15,000 shoppers, says sales of fresh vegetables were up 6.8% last year, compared with just 2.6% for canned vegetables and 1.9% for frozen. Expensive chilled meals were up by 8.1%, compared with just 1.6% growth in frozen ones.

Those tastes started with rich-but-busy customers, but the supermarkets now find that other people are shopping the same way, says Ben Britz, an analyst at Morgan Stanley. A preference for spontaneous social life strengthens the trend. “The notion of sitting down and working out a menu plan for the week leaves most people cold,” says Mark Price, marketing director at Waitrose. Instead, they buy more perishable food in smaller quantities.

The supermarkets face little competition from the independent businesses who still run more than half the convenience stores. An average store charges 15% more than a supermarket, while a Tesco Express or Sainsbury's Local charges only 3-4% extra. As a result, independent stores are disappearing at the rate of almost one a day, according to IGD, a food and grocery think-tank, with many joining franchise groupings like SPAR to take advantage of somewhat increased purchasing muscle.

David Rae, head of the convenience stores' lobby group, says that in many areas the only choice will soon be between a different sized outlet of one of the major supermarket chains. But for the growing number of shoppers whose baskets contain only a packaged salad and a microwavable meal, that may sound just fine.

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Housing market

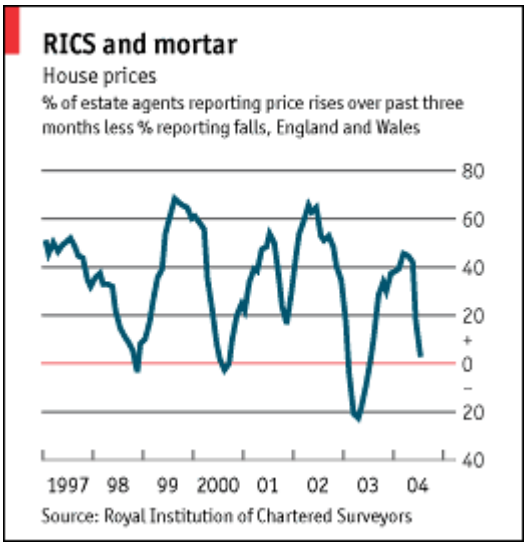
Calling the turn

Aug 19th 2004
From The Economist print edition

Has the Bank of England got it right?

THERE was no dissenting vote when the Bank of England decided to raise interest rates from 4.5% to 4.75% earlier this month, according to minutes of the meeting released on August 18th. The nine members of the Bank's monetary-policy committee did not consider the case for a larger increase.

The minutes chime with the strikingly dovish tone of the Bank's quarterly *Inflation Report*, issued on August 11th. For the first time this highlighted GDP and inflation forecasts based on the market's predictions for the Bank's base rate rather than those assuming that it stays unchanged. That presentational change reinforced a clear message: the Bank thinks it has completed most of its monetary tightening from the low of 3.5% late last year. As little as one further quarter-point rise in rates, to 5.0% later this year, may be sufficient to meet the government's annual inflation target of 2% over the next two years.



The Bank now thinks the economy is operating at capacity, so this benign outlook for inflation hinges upon a predicted slowdown in GDP growth from its recent rapid pace of nearly 4% a year to a below-trend 2% in 2006. This in turn rests heavily upon a moderation in consumer-spending growth as the housing market cools down. The Bank's main projection is for a sharp deceleration in house-price inflation.

Shoppers already appear to be losing some of their zest according to the latest figures. These show that retail sales fell by 0.4% in July compared with June, although they were still a hefty 6.6% higher than a year ago. Further restraint by consumers depends a lot on what happens to house prices. The Bank has been forecasting a slowdown for quite some time, but so far it hasn't materialised. According to the Nationwide building society, house prices rose by 2.1% in July, pushing the annual rate up to 20.3%. The Halifax index showed prices rising by a smaller 1.3% in July but its annual rate increased to 22.1%.

However, other signs suggest the Bank may shortly be proved right. A survey of estate agents by the Royal Institution of Chartered Surveyors (RICS) suggests an abrupt turn in the housing market. In July, the proportion reporting price increases exceeded the proportion reporting price falls by only 3%—down from majorities of 17% in June and 42% in May. Sentiment is particularly gloomy in London, the south-east and south-west, where a majority of agents think prices are declining rather than rising.

The RICS report is significant because it captures current market conditions. According to Robert Barrie of CSFB, an investment bank, the survey's figures are consistent with annual house-price inflation slowing to around 5% early next year.

But the Bank's soft-pedalling strategy could be storing up trouble. If home-buyers think that interest rates are close to their peak, they may regain their confidence and the housing market could then take off again. Since house prices are already well above their long-run sustainable values, that would make the eventual crunch more dangerous.

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Farm subsidies

Last of the summer whine?

Aug 19th 2004
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Farmers face a new regime: subsidy for land, not crops

THE rain-battered harvest is nearly in —the last one, for most British farmers, that will bring them subsidies dependent on just what they produce or how much of it. From next January 1st, no more “arable area payments”, “suckler cow premium” or “beef national envelope”: today's swarm of schemes will be swept into a “single farm payment”. The shift will bring British farming closer to the market. In time, it may change the face of Britain too.

Subsidy will continue, and at much like recent levels—£2.8 billion last year. But thanks to European Union (EU) reform decisions a year ago, which Britain, unlike some countries, chose to put into effect as soon as possible, the money will no longer be linked to particular products, output levels, or even farming at all. Instead, it will be based solely on land area. British farmers, contrary to myth, are already highly market-oriented. From 2005 they will have to be entirely so.

That's a big change from the days when the EU guaranteed high prices for every tonne of almost anything but fruit and vegetables. That system has been eroding since 1984, but the new single payment breaks the last link (with odd exceptions such as sugar beet) between subsidy and output. It will start with the past: the farm's total average subsidy, per hectare, under all schemes, in 2000-02 (or, for dairy farmers, the annual value of their milk quotas in 2005). But by 2012 all English farms will get a standard flat rate: £210-230 or so per hectare in lowland areas.

Despite this gentle transition there will still be winners and losers (big ones, potentially, in Wales and Scotland, which will therefore stick to each farm's “historic” levels). Horticultural land, now unsubsidised, will in time get the full flat rate. English dairy farmers, already hurt by low prices, stand to lose. So do intensive grain-growers, who have done well out of subsidies; and the beef barons, using little land but lots of bought-in feed. Less intensive farmers will gain, especially in the hills.

Some questions remain unanswered. What about rich hobby farmers who have a few decorative fields around their mansions? Or “horseyculture”, the (now unsubsidised) pastures used for family ponies? There is still much confusion about landlord and tenant, especially for land recently or soon to be let: who will get how much? And no one knows how the new market in tradable subsidy entitlements will work, or the effect on land prices.

But one broad result is clear. Subsidy linked to the environment has already shot up: it was nearly £280m last year, against £45m ten years before. Now the new farm payment itself will depend on farmers' compliance (self-declared, admittedly) with EU environmental, health and other rules. Many farmers plan to earn an extra £30 a hectare by joining a basic environmental scheme, for example leaving the edges of fields unploughed, to help bugs and the birds that feed on them.

Change could go much further. Some farmers will simply let land lie fallow, maybe even the whole farm: to get subsidy, all they will have to do is to keep the land in “good agricultural and environmental condition”. That's not cost-free, but it is easier than the hassle of ever-changing weather, prices and tastes.

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Private universities

A new deal

Aug 19th 2004
From The Economist print edition

A private-sector deal opens Britain's higher education business

BRITAIN has two big higher-education institutions outside the state sector. Now they are joining forces. One is the University of Buckingham, an operation founded on free-market principles which eschews state funding for teaching and the planned-economy controls that go with it. The other is BPP, a publicly-quoted company that is the country's largest provider of professional training for lawyers, accountants and solicitors and the like. It would like to be a for-profit university on American lines, but is held back by legal restrictions on degree-awarding powers.

The Economist can reveal that BPP and Buckingham have reached agreement "on all the main questions", according to Terence Kealey, Buckingham's vice-chancellor. BPP will launch a bunch of hybrid postgraduate courses next academic year, in accountancy, tax, law, finance and actuarial studies. These will bring both the relevant professional qualification, and a master's degree awarded by Buckingham. Students may study at one of BPP's 30-odd centres, or at Buckingham's leafy campus.

BPP qualifications already include degrees awarded through deals with three public universities. But Carl Lygo, head of the company's law division, says "Buckingham are more practical and professional." Unlike other universities, they don't find BPP threatening, he says.

The deal underlines a recent revival in Buckingham's fortunes. Lack of cash, an inconvenient location and weak leadership meant that it largely failed to dent its publicly-subsidised competitors. But in recent months it has recruited the country's best-known educational researcher, Alan Smithers, from Liverpool University, and is now raising money to start a private medical school, Britain's first. The BPP deal means welcome cash and extra credibility; it will also strengthen the business school, a key bit of Buckingham's new strategy.

"We are focusing on these vocational courses because they are what people are prepared to pay extra for. The huge class sizes at the state universities leave people very dissatisfied," says Mr Kealey.

That will be a nasty shock to the state sector. Many public universities depend heavily on profits made from the sort of courses that BPP and Buckingham will now be offering. Change in British higher education is usually frustratingly glacial. This deal, first conceived less than three months ago, is an exception.

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Hewlett-Packard

Losing the HP way

Aug 19th 2004 | SAN FRANCISCO
From The Economist print edition

AP

Two years after Carly Fiorina pulled off a transforming merger, Hewlett-Packard looks huge, frail and confused

Get article background

IN A job that requires being tough and even ruthless, also being one of the most charming bosses in your industry does not hurt. Carly Fiorina, the chief executive of Hewlett-Packard (HP), has that advantage. Attractive, stylish, a good conversational partner on topics ranging far beyond technology—she was a medievalist at college—Ms Fiorina stands out in the geeky, male world of computing. With so much yin to dazzle and distract, her aggressive yang instincts pack that much more force. Thus, in 2002, she pulled off one of the most controversial mergers ever, of HP and Compaq, over the bitter opposition of Walter Hewlett, a son of one of HP's founders, and despite a cliff-hanging 49% of HP's shareholders voting against it.

Her problem ever since has been to justify the beast she thereby created. HP's shares are worth less today than on the day before the merger was announced or on the day it closed. A consensus has emerged in the industry that the new HP, the tech industry's most sprawling conglomerate, has lost its focus and is being squeezed between two formidable rivals with much clearer business models, Dell and IBM. Where Dell stands for cheap, simple boxes in an industry that is commoditising, and IBM stands for patching together lots of fiddly subsystems in an industry that remains ridiculously complex, HP seems a lukewarm compromise.

As if to prove that thesis, HP announced on August 12th that its profit for the latest quarter, at $846m, was less than a year earlier and far below what Wall Street had been expecting. On the same day, Dell said that its quarterly profit was up by 29%, while IBM, which had already announced a 17% increase in quarterly profit, added that it would hire 18,800 people this year.

Stuck in the middle with Carly

Ms Fiorina reacted by giving another glimpse of her tough side, firing three top executives on the spot, and stubbornly sticking with her strategy. For two years, she has, time and again, been intoning the same script. HP is far from “stuck” between Dell and IBM, she asserts. Instead, Dell, famous for its supply chain rather than its patents, represents “low tech and low cost”, while IBM, best known for its

armies of technology consultants, peddles “high tech and high cost”, which leaves only HP to offer “high tech and low cost” and therefore “the best customer experience”. Yet the pressure is starting to show. In a recent speech, Ms Fiorina started 11 sentences with an irritable “Frankly,...”.

Her problem, in a nutshell, is that HP is trying to be all things to all kinds of customers, and is leaving more and more of them plain confused. HP dominates in the market for printers, both laser and inkjet, and both for consumers and companies. It is also strong in handheld computers and some other consumer electronics items, such as digital cameras. In desktop personal computers and notebooks, HP runs neck-and-neck with Dell as the world's biggest supplier.

But in enterprise computing, from storage systems to servers, the picture gets more complicated. Ms Fiorina's public-relations minions regularly circulate long and tedious lists of obscure sub-segments of the market in which HP has the largest market share—“fault-tolerant systems”, “external storage systems”, “tape drives”, “virtualisation technology” and so on. Being big in so many different areas, they argue, means that HP is the “leader” and vindicates the merger.

The opposite is more likely. HP's profits disappointed precisely because the jumble of its business units selling to companies made a loss of $208m for the quarter. In each area, it turns out, HP is fighting separate wars against different and fiercely focused competitors—EMC in storage hardware, Veritas in storage software, StorageTek in tape drives, Sun Microsystems in Unix servers, IBM in consulting services, and so on. The only way that HP manages to stay in so many games, at least according to Dell, is by leaving its profit margins on the table for others—and above all for Dell itself.

This leaves HP in a most undesirable place in today's technology industry. Three years after the dotcom bust, corporate spending on technology is this year showing the first signs of growing again. But the improvement is almost trivial, and mostly limited to sub-segments such as security and integration software. “This is the recovery; enjoy it,” recently sneered Larry Ellison, the boss of Oracle, the world's second-largest software company. All this means that only the strongest, most focused technology companies will benefit. HP does not seem to be one of them.

Yet HP's situation may not be entirely hopeless. Steven Milunovich, an influential analyst at Merrill Lynch, argues that, amid all the bitter fighting of the past three years, Ms Fiorina has simply become confused between two separate issues. One question is whether HP and Compaq, each weak in computers at the time of the merger, needed each other to bolster their position. The answer to that may well be yes. Quite another question is whether this means that HP must now forever remain a company that makes computers, printers, cameras and a host of other gadgets, as well as a company that sells to big companies, small companies and consumers. The answer is almost certainly no.

Ms Fiorina's best option is to address the “conglomerate discount” in HP's share price—in other words, to break up her company, says Mr Milunovich. Many of HP's investors would prefer to own only its stellar printing and imaging business, which need not apologise to anyone. This would also free the printer business to parry the distant threats from rivals such as Lexmark and Dell.

The case for being beta female

The remaining computer and storage businesses could then be further divided by customer focus—corporate versus consumer—or merged with rivals. The result would be several well-targeted companies that would either be genuine leaders (printers) or potentially profitable runners-up in corporate computing, the “Avis to IBM's Hertz”, as Mr Milunovich puts it.

When this idea was formally put to her at an analyst meeting in June, Ms Fiorina responded by ignoring it, commenting only that HP was misunderstood by Wall Street—ie, that the market was wrong. It is unlikely that Ms Fiorina, who in her previous career oversaw the spin-off of Lucent from AT&T, is a stranger to the theory of corporate clarity. Could it be that years of conflict in testosterone-filled rooms have left her afflicted with that psychology so common among bosses of the other gender: the compulsion to rule the roost?

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The business of death

Stiff competition

Aug 19th 2004 | NEW YORK
From The Economist print edition

A cheaper way to face the final curtain

DEATH does not come cheap in America. The Federal Trade Commission (FTC) reckons that the cost of a no-frills burial is $6,000. Extras such as flowers and a limousine can add thousands of dollars to the bill. The biggest expense is the casket which, in fancy mahogany or copper, can cost as much as a family car. Not so at Costco, a warehouse-style retailer that sells vats of mayonnaise and cases of tinned tomatoes at bargain prices to America's middle classes. Starting on August 16th at two locations in Chicago, Costco began piloting the sale of discounted coffins.

Costco's coffins come in six models and several finishes, including gold, lilac and, *The Economist*'s favourite, Neapolitan blue. As with the tyres, plumbing fixtures and other big items that the retailer sells, Costco does not keep its coffins in stock. Instead, shoppers browse casket samples at a kiosk near the shop entrance. The price, including delivery to a nearby funeral home, is $799.99. The same coffin from a traditional funeral-services firm would cost $3,500-5,000, says Bob Nelson of Costco. “This is an industry that traditionally people get ripped off in.”

That has long been the view of the FTC, which in 1984 introduced strict rules governing the sale of funeral goods and services in America. Funeral providers must give customers a detailed price list of all they sell. The rules prohibit funeral providers from lying to customers about the need to buy concrete grave vaults, expensive caskets for cremation and embalming services when refrigeration would do just as well. An FTC rule introduced in 1994 banned funeral providers from charging an extra fee to customers who buy their caskets elsewhere.

This last change encouraged new, specialist high-street and internet casket retailers. ABC Caskets, a Los Angeles-based coffinmaker, has a lock on the Hollywood market: its discounted coffins appear in “Six Feet Under”, a popular TV series about undertakers. D-I-Y enthusiasts, meanwhile, can buy plans for caskets and urns from firms such as MHP Enterprises, and build their own. MHP's line starts with the modest and unchallenging “simple pine coffin plan”, which, for just $14.95, helps you build a final resting place which looks surprisingly like a croquet-set box.

Despite the promptings that funeral providers must give their customers to shop around, most Americans resist bargains for their loved ones and continue to buy fully-priced caskets from traditional undertakers. America's biggest funeral firms, such as Stewart Enterprises and Service Corporation International, say that average revenues per customer for traditional burials continue to rise, albeit modestly. (With the growth in deaths per year slowing in America and more people choosing a cheap cremation, these firms are struggling with falling overall revenues, however.) Costco may find that its customers do not want the final goodbye to be a good buy.

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Drug pricing

Aussie rules

Aug 19th 2004
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The global significance of a row over drug prices in Australia

GEORGE BUSH was supposedly rewarding his ally, John Howard, for his support over Iraq. Instead the president landed the Australian prime minister—who, like Mr Bush, is embroiled in a tough re-election battle—in political hot water with the bilateral trade agreement between America and Australia that he signed on August 3rd. Although the agreement will bring tariff reductions that could boost Australia's GDP by up to 1% a year, Australian hackles have been raised by an unusual clause in the agreement about drug prices—a clause that America would dearly love to replicate everywhere.

According to Mr Howard's critics, the agreement will mean higher drug prices in Australia—where prices are currently much lower than in America. Though denying it would raise prices, Mr Howard accepted opposition amendments in order to get the agreement through parliament on August 13th. As a result, America may, but probably will not, renege on the deal.

AP

What drug industry lobby, John?

Currently, Australia's Pharmaceutical Benefits Scheme (PBS)—much like similar bodies in many other countries—assesses every drug for effectiveness and price before deciding whether the government will pay for it. Under the new trade deal, if the PBS decides not to pay for a drug, its manufacturer can now ask the head of a new review organisation to obtain and publish an independent expert's second opinion. As the PBS is free to ignore the review, the process will not drive up prices, says Mr Howard. But if so, why did America want that clause? The boss of one of the world's biggest drug firms says that the right of appeal will at least introduce valuable transparency into the PBS process. And yet there seems more to it than just this. According to a recent article in the *Medical Journal of Australia*, a provision of the agreement could let America retaliate if an American drug is not approved.

The agreement also bars Australia's patent agency from approving generic versions of a drug while a patent application is pending. This could potentially allow American drug firms to use a tactic known as “evergreening” to delay competition from generics. In America, as the patent on a drug's active ingredient expires, its manufacturer will typically file (allegedly) frivolous patent applications based on its delivery method or capsule. As a result, it enjoys extended monopoly protection while the applications are considered.

The opposition Australian Labor Party insisted on anti-evergreening amendments in exchange for its support for the agreement. These require drug companies trying to prevent generic entry to their markets to submit a certificate saying that their application is filed in good faith and has “reasonable prospects of success”.

This seems unlikely to deter the drug firms. If the certificate is found to be “false or misleading”, drug firms can be fined—but only up to $7.2m, peanuts to most of them. And what is false or misleading? “It's too easy for a law firm to give an opinion to a drug company, ‘yes, there is some reasonable prospect of your patent being upheld.’ That could be a one-in-ten chance,” says Kevin Outterson, a law professor who has studied the American-Australian trade agreement.

Mr Outterson is sceptical about Mr Howard's claims that the deal will not raise drug prices. “A betting man would predict that three to five years from now, Australia's PBS prices will be higher. Howard claims

to have snookered [the industry] on this one, but I have rarely seen them lose a sophisticated game like this," he says. If drugmakers were able to extend patents on the five drugs on which the PBS spends most, they would be paid an extra $1 billion in 2006-09, according to the Australia Institute, a think-tank.

Why is America fighting so hard for the drug firms? High drug prices in America have become a big political stick with which the Democratic presidential candidate, John Kerry, is bashing Mr Bush. American politicians have long complained that Americans bear a disproportionate share of the cost of developing new drugs, that are then sold much more cheaply to foreign free-riders. The drug firms are a powerful lobby in Washington, DC. If he is to crack down on prices at home, Mr Bush feels he must appease the drug firms by—don't tell Mr Howard—helping them to earn more profits abroad.

America now seems likely to accept the amendments because, even if Australian drug prices remain only 25% of America's, the agreement sets a precedent that America can use in negotiations with bigger fish, such as the European Union and Japan. Miles White, the new head of America's Pharmaceutical Research and Manufacturers Association, calls the agreement a "first step" towards addressing "the harmful health and economic consequences of foreign price controls."

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Sportswear

No sweat

Aug 19th 2004
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Campaigners against clothing sweatshops go to the Olympics

EPA

The visually-enhanced Thorpedo

ADIDAS may be upset that the star Australian Olympic swimmer whom it sponsors, Ian “the Thorpedo” Thorpe, has cast doubt on the firm's claims that its new swimsuits “help you swim faster”. Mr Thorpe reckons that most of the recent advances in swimsuits have been “visual”. But several other top sporting-goods brands have a different reason to fret. The shirts and shoes they make for athletes are the target of perhaps the biggest-ever crusade against sweatshops. The Play Fair at the Olympics Campaign was launched jointly in March by Oxfam, Global Unions, an international confederation of trade unions, and the Clean Clothes Campaign. It juxtaposes the ideals of the Olympics with the realities of the sportswear industry. And big brands such as Puma and Umbro are starting to sweat.

A report by the campaigners describes labour problems allegedly arising from the industry's long and winding supply chains. Big companies outsource manufacturing through contractors, then subcontractors, and fierce retail competition translates into a squeeze on factories in Bulgaria, China, Indonesia or wherever. Deadlines are tighter, and sportswear retail prices have slid by 5-10% in the past five years. Yet the big-brand companies still claim to have proper codes of conduct for labour practices. Seven-day weeks and 18-hour days? Oh, those are the suppliers' fault.

In the general sweat of the clothing industry, why target sportswear? Because it has a few globally known companies with big market shares. The biggest, Nike, Adidas and Reebok, which together have nearly 15% of the $58 billion market, have already been “named and shamed”. After the anti-sweatshop campaigns of the late 1990s, all three joined the Fair Labour Association, which sends inspectors, unannounced, to check on working conditions in factories. But, in an interesting illustration of how modern campaigns by activists against companies can gather momentum, the top-tier companies now complain that lesser ones get away with poor labour practices, and so impede progress in the whole sector. The Olympic campaigners are therefore targeting second-tier brands such as Puma, Mizuno, Umbro and Asics. Several of these have begun talks with the campaign and with the International Labour Organisation, an arm of the United Nations.

The campaigners sent the International Olympic Committee a petition that it said had over 500,000 signatories, calling on the IOC to ensure that products displaying its five-ring logo are made by companies that observe “fair labour standards”. The IOC has ducked, but the European Parliament has passed a resolution supporting this aim, and a bill before the United States Congress seeks to compel that country's Olympics committee to do so. How much consumers care, if at all, remains unclear.

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Business in China

Manacling the mandarins

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China's powerful bureaucrats have lost a lawsuit

AN OBSCURE legal dispute about trademarks may signal a turning point in China's long march toward the rule of law. In the past month, Chinese legal experts have been unusually excited by a court judgment, little noticed outside the country, whereby an arm of China's national government was successfully sued by a private firm in a Chinese court. This may be the first time that any agency of the national government has lost a lawsuit, and the judgment is a direct result of recent legal changes brought about as a result of China joining the World Trade Organisation (WTO) in 2001. Similar lawsuits challenging other arms of the government are likely. If some of these succeed, China's courts could end up providing an independent check on the almost unfettered power of bureaucrats, transforming the legal landscape for firms operating there.

The decision, issued on July 22nd by the Beijing No. 1 Intermediate People's Court, concerned an application by the Nanjing Zishi Law Firm to register a trademark on behalf of a Chinese supplier of agricultural products. The law firm was turned down flat by the government's trademark bureau. The firm's appeals to more senior levels in the state administration were also refused. So last October the law firm took the unheard-of step of suing the trademark bureau.

The bureau argued that only trademark agencies could represent clients applying for trademarks, and that the trademark law made no mention of law firms acting in this capacity. But the court relied on a basic principle of most established legal systems, that what is not specifically prohibited should be allowed, and ruled that the trademark law did not prohibit lawyers from acting as agents and that, moreover, a 1997 law governing lawyers said that they could provide any legal service, and that filing trademarks was certainly a legal service. The trademark bureau is expected to appeal to a higher court, but lawyers think it will lose there as well.

In a country where trademarks are still widely violated, the case may seem a trifle esoteric to many business people. But in fact it fits a pattern all too typical across China's vast government bureaucracy, in which agencies blithely issue self-serving regulations. Until now, these have been free of any independent review. One reason the trademark bureau was reluctant to let a law firm file a trademark application was that this business has been confined to trademark agencies, most of whose fees flow to the bureau's parent ministry.

Also significant, say Chinese lawyers, is the fact that the Beijing court seemed to sit on the case until a new administrative licensing law took effect on July 1st. This was passed as part of the Chinese government's efforts to meet WTO requirements and to rein in its own bureaucrats by making administrative procedures more transparent and accountable. The law seems to have had an instant effect, emboldening the Beijing judges to rule against the trademark bureau. If other judges follow their lead, China's bureaucrats will no longer be a law unto themselves.

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Executive pay in Germany

Keeping stumm

Aug 19th 2004 | FRANKFURT
From The Economist print edition

On disclosing pay, most German firms defy the corporate-governance code

WHAT are Germany's corporate fat cats paid? Alas, only nine of Germany's top 30 listed firms disclose how much they pay, individually, their top executives—a subject of growing interest in the country, especially since the recent Mannesmann trial drew attention to the issue of executive remuneration. That is despite all 30 signing up two years ago to a corporate-governance code that strongly recommends such a pay breakdown.

Germany is the laggard among the developed countries of Europe—behind Britain, France, Ireland, the Netherlands and Sweden, which make disclosure of the pay of individual members of the board of directors a legal or stock-exchange requirement, as does America. Even Italy demands it for prospectuses. German law demands only the publication of an aggregate figure for the entire board.

Brigitte Zypries, Germany's justice minister, has threatened to put the requirement for individual disclosure into law if the big 30 firms do not comply by next summer. Hans Eichel, the finance minister, says that he will require it of government-owned firms, such as Deutsche Bahn and KFW, in their 2004 annual reports. Horst Köhler, Germany's president, added his voice to those of union leaders and (some) company executives calling for voluntary compliance. This week, Michael Diekmann, boss of Allianz, bowed a little to the pressure and disclosed his salary, but not those of his fellow board members.

The excuses made by non-compliant firms, such as Allianz and DaimlerChrysler, are unconvincing: it would lead to a “levelling” of pay among its executives; and it conflicts with a German board's “collective responsibility”. Making both arguments at once—as Daimler does—is especially absurd: if they have collective responsibility, surely executives should know what their colleagues are paid?

Paul Achleitner, a board member of Allianz, sits on the Cromme Commission, which designed the corporate-governance code. So does Wendelin Wiedeking, chief executive of Porsche, which rejects disclosure on levelling and privacy grounds. But both sit on the commission in a personal not a company capacity, it seems.

Animosity between the European Commission and Germany over standards of governance is brewing on two fronts. One commission consultation paper recommends a “cooling-off period” of five years before an executive of a firm moves up to its supervisory board. This is a full-frontal assault on standard German practice: former chief executives of 16 of the top 30 companies moved straight up and now run their supervisory boards. Meanwhile, an EU-inspired “company-law action plan” is expected to require a full breakdown of executive pay in all member states. And why not?

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European telecoms

The broader art of deregulation

Aug 19th 2004 | PARIS
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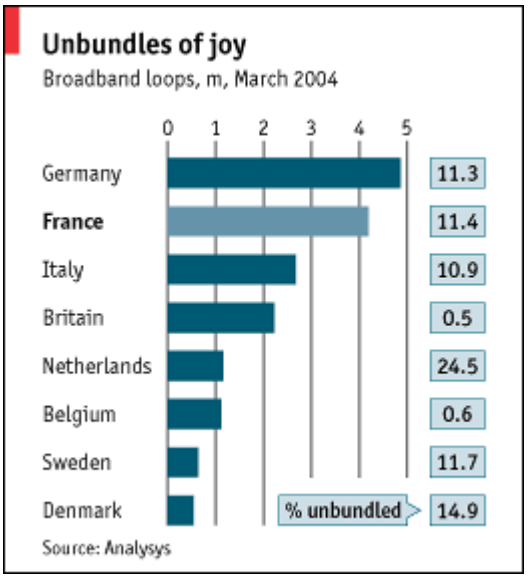
Surprisingly, Europe's coming leader in broadband is France

WHEN it comes to promoting vigorous free-market competition, France does not spring to mind. Yet in broadband telecoms, at least, French consumers enjoy one of the most competitive markets in Europe. A new report from Ovum, a consultancy, calls France's performance “stellar” and predicts that it will soon overtake Germany as the European country with the most broadband-enabled telephone lines.

The champion of France's broadband boom is Iliad, a young telecoms firm that offers some of the most advanced services in Europe. For a mere €30 ($37) a month, Iliad's service, sold under the (not entirely accurate) “Free” brand, provides high-speed internet access, digital television and free nationwide phone calls. This is less than half the price of a similar bundle elsewhere in Europe—in the few countries where it is even available. No wonder Iliad has become France's second-largest broadband-internet provider, having signed up 768,000 customers since launching its “triple-play” combination in October 2002.

Iliad's success owes much to Autorité de Régulation des Télécommunications (ART), France's telecoms regulator. ART has been getting tough with France Telecom, the dominant, partly state-owned phone company. Three years ago, ART forced the incumbent to allow its rivals to use the “local loop”—copper wires that run from telephone exchanges to homes. ART insisted that this “unbundling” happen at some of the lowest prices in Europe.



France had the highest rate of broadband growth in Europe last year. It has the second-largest number of unbundled local loops in Europe and, proportionately, one of the highest (see chart). Unbundled loops free rival telephone firms from the grip of the incumbent. New entrants, such as Iliad, connect the lines directly to their own equipment, inside local exchanges.

This takes time and money: two years and over €100m in Iliad's case. But then a firm can provide TV, internet and telephone services to its customers over an ordinary phone line—which its rivals cannot do. Indeed, Iliad's reputation now precedes it. Under half of its customers use unbundled lines: the rest were attracted to the firm by its record of innovation.

Some industry insiders mutter that ART's intervention unfairly favours new entrants. Lower prices for the local loop may discourage the development of alternatives to the phone network. Why build a competing infrastructure when you can hire the existing one on favourable terms? Yet the folks at ART seem pleased with themselves. Consumers are happy too.

The clement regulatory environment has allowed Iliad to develop a nifty vertically integrated business model. Iliad designs its own set-top boxes, runs its own optical network around France and has even built the kit that sits in the local exchanges. In the age of outsourcing, this do-it-yourself approach may seem untrendy but it lets the firm save money and cut prices for consumers, says Olivier Rosenfeld, Iliad's finance chief. Amazingly, in the midst of a land grab for customers, Iliad is already making money, turning a €34m profit on revenues of €293m in 2003.

So successful has been France's regulatory intervention that other regulators are now following suit—at least in Europe. According to the Paris-based OECD, prices for unbundling have fallen in ten European

countries since 2002, in some cases even making French levels now look relatively pricey. (In America, unbundling has become quite controversial. State regulators have fought local phone companies to encourage local-loop unbundling—but with little success. The Federal Communications Commission has, as ever, been split on the matter.) In Britain, once in the vanguard of telecoms deregulation, high prices meant that only 8,000 local loops (out of 23m) were unbundled at the end of 2003. In May, pressured by regulators, BT, the incumbent, said it would cut prices for unbundled loops by up to 70%, moving in line with the European average. France's telecoms market, like its trains, seems to have overtaken Britain's.

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Corruption in Italy

Dog bites man

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An arrest revives the spectre of corruption at ENI

BACK to bribesville? This month a manager at EniPower, the power subsidiary of ENI, was arrested in connection with backhanders on contracts. Founded in 1953, ENI was the Italian state's attempt to challenge the oil majors. Deeply involved in the massive corruption scandal known as *tangentopoli* (bribesville) of the early 1990s, it was floated in November 1995. The prospectus told investors of senior managers indicted on charges that included false accounting, corruption and the misappropriation of funds. A chairman who had profited from what was called the “mother of all bribes” had committed suicide in July 1993.

The magistrates in Milan have not yet completed digging in the new case, but are already investigating 50 people and 20 companies. At an emergency board meeting on August 10th, four days after the arrest of the EniPower manager, ENI endorsed his immediate sacking, affirming that any staff found not to have complied with the group's code of conduct would go the same way. The board set up a task-force to check on all supply contracts awarded since 1998 by EniPower and Snamprogetti, an engineering subsidiary. Expressing complete confidence in the magistrates, it instructed the chairmen of its two subsidiaries to co-operate fully with them.

The largest firm on Milan's stockmarket, ENI could hardly have done otherwise. Its shares—70% now in private hands—are also listed in New York. Foreigners own around one-third. The board had to reassure the market, which has never found claims about better behaviour in corporate Italy entirely convincing. There was a similar scandal last year at Enelpower, a subsidiary of Enel, a large state-controlled power firm. Investors may also recall that in 2001, soon after taking power, Silvio Berlusconi's government gave a fillip to the would-be corrupt with legislation downgrading the crime of false accounting.

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About sponsorship

Face value

Profits and poverty

Aug 19th 2004
From The Economist print edition

C.K. Prahalad thinks there can be a win-win relationship between business and the poor

"IF WE stop thinking of the poor as victims or as a burden and start recognising them as resilient and creative entrepreneurs and value-conscious consumers, a whole new world of opportunity will open up." That "simple proposition" begins a controversial new management book that seems destined to be read not just in boardrooms but also in government offices. "The Fortune at the Bottom of the Pyramid. Eradicating Poverty Through Profits" (Wharton School Publishing), is essentially a rallying cry for big business to put serving the world's 5 billion or so poorest people at the heart of their profit-making strategies. It has already been praised by everyone from Bill Gates—"a blueprint for fighting poverty"—to a former American secretary of state, Madeleine Albright—"if you are looking for fresh thinking about emerging markets, your search is ended."

Its author, C.K. Prahalad, is accustomed to rave reviews. (The C is for Coimbatore, the Indian town of his birth, the K for Krishnarao, his father's name.) After becoming a management professor at the University of Michigan via a job at Union Carbide and study at the Indian Institute of Management and Harvard, he wrote "Competing for the Future" (Harvard Business School Press) with Gary Hamel in 1994. This tome was regarded as perhaps the best business book of the 1990s—an accolade that, admittedly, may be less than it sounds, given the amount of rubbish published by the business-book trade (see article).

As the two gurus searched for their next hit, Mr Hamel stumbled across Enron, a then-thriving energy conglomerate that he eulogised in "Leading the Revolution" (Harvard Business School Press). Mr Prahalad, by contrast, "after searching for a couple of years, saw that the big idea was creating wealth at the bottom of the pyramid". He has been evolving his ideas about how firms should focus on the bottom of the pyramid—a phrase he shortens to BOP, to contrast with those wealthy folk at the TOP—since 1997, despite a spell running Praja, a business-activity-monitoring software firm that later had to be sold when it could not raise the capital it needed in the aftermath of the tech bubble. "Badly timed, but taught me a lot," claims Mr Prahalad.

He is a fierce critic of traditional top-down thinking on aid, by governments and non-governmental organisations alike. They tend to see the poor as victims to be helped, he says, not as people who can be part of the solution—and so their help often creates dependency. Nor does he pin much hope on the "corporate social responsibility" (CSR) programmes of many large companies. If you want serious commitment from a firm, he says, its involvement with the poor "can't be based on philanthropy or CSR". The involvement of big business is crucial to eradicating poverty, he believes, but BOP markets must "become integral to the success of the firm in order to command senior management attention and

sustained resource allocation."

Mr Prahalad reckons that there are huge potential profits to be made from serving the 4 billion-5 billion people on under $2 a day—an economic opportunity he values globally at $13 trillion a year. The win for the poor of being served by big business includes, he says, being empowered by choice and being freed from having to pay the currently widespread "poverty penalty". In shanty towns near Mumbai, for example, the poor pay a premium on everything from rice to credit—often five to 25 times what the rich pay for the same services. Driving down these premiums can make serving the BOP more profitable than serving the top, he argues, and points to a growing number of leading firms—from Unilever in India to Cemex in Mexico and Casas Bahia in Brazil—that are profiting by doing precisely that.

BOP till you drop

But to be profitable, firms cannot simply edge down market fine-tuning the products they already sell to rich customers. Instead, they must thoroughly re-engineer products to reflect the very different economics of BOP: small unit packages, low margin per unit, high volume. Big business needs to swap its usual incremental approach for an entrepreneurial mindset, because BOP markets need to be built not simply entered. Products will have to be made available in affordable units—most sales of shampoo in India, for example, are of single sachets. Distribution networks may need to be rethought, not least to involve entrepreneurs from among the poor. Customers may need to be educated in how to consume, and even why—about credit, say, or even about the benefits of washed hands. The corruption now widespread in poor countries must be tackled (about which Mr Prahalad has penned a particularly useful chapter).

There are plenty of sceptics. Are the opportunities for profitable product re-engineering really as common as Mr Prahalad thinks? How much can private firms accomplish given inept or corrupt governments in many poor countries? "There is much less scepticism now than when I first started talking about the BOP," retorts Mr Prahalad. What the leading firms are grappling with now, he says, is not whether there are profits to be made, but how to serve the BOP on a big enough scale, and how to transfer what works from one part of the world to another.

Another challenge will be to persuade development experts to support a profit-driven strategy. Mr Prahalad worries that firms may be deterred from BOP strategies by fear of attracting criticism from activists. If a large international bank were to start lending to the poor at interest rates, reflecting higher risks and start-up costs, of say 20% (compared with around 10% in rich countries), "the whole anti-globalisation lobby would probably be against it. Yet the alternative is for the poor to borrow at 500% from a money lender. Whose side are the activists on?" If you are on the side of the poor, he says, "surely you need to help get rates down from 500% to 20%. After that, you can work on getting them from 20% to 10% like in the rich world."

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About sponsorship

China's environment

A great wall of waste

Aug 19th 2004 | BEIJING, GUANGZHOU, HONG KONG, SHANGBA, SHANGHAI AND TAIHE
From The Economist print edition

ROPI

China is slowly starting to tackle its huge pollution problems

Get article background

PLUGGING a cigarette into his mouth, He Shouming runs a nicotine-stained fingernail down a list of registered deaths in Shangba, dubbed “cancer village” by the locals. The Communist Party official in this cluster of tiny hamlets of 3,300 people in northern Guangdong province, he concludes that almost half the 11 deaths among his neighbours this year, and 14 of the 31 last year, were due to cancer.

Mr He blames Dabaoshan, a nearby mineral mine owned by the Guangdong provincial government, and a host of smaller private mines for spewing toxic waste into the local rivers, raising lead levels to 44 times permitted rates. Walking around the village, the water in the streams is indeed an alarming rust-red. A rice farmer complains of itchy legs from the paddies, and his wife needs a new kettle each month because the water corrodes metal. “Put a duck in this water and it would die in two days,” declares Mr He.

Poisons from the mines are also killing the village's economy, which depends on clean water to irrigate its crops, says Mr He. Rice yields are one-third of the national average and nobody wants to buy the crop. Annual incomes here have been stuck at less than 1,500 yuan ($180) per person for a decade, almost three times lower than the average in Guangdong province. The solution to Shangba's nightmare would be a local reservoir, but that idea was abandoned after various tiers of government squabbled over the 8.4m yuan cost.

Some 200km (124 miles) farther south and several decades into the future sits the Taihe landfill plant. Built for 540m yuan by Onyx, a waste-management company that is part of Veolia, a French utility, it has handled all of Guangzhou city's solid waste for the past two years. Each hour 140 trucks snake into the site, bringing 7,000 tonnes of rubbish a day from the 9.9m inhabitants of Guangdong's capital. In October delegates from 300 other municipalities will visit Taihe, promoted by central government as a role model of technology.

Smart cards record each truck's load, since Onyx charges by weight. Unrippable German fabric lines the crater into which the waste is dumped, stopping leachate—a toxic black liquid—from leaking into the groundwater, as it does at almost all Chinese-run sites. Most landfill in China is wet (solid rubbish, such

as old TVs, is scavenged), and the Taihe plant collects a full 1,300 tonnes of the black liquid daily. Chemical and filtration systems to neutralise it are its biggest cost. Expensive too is the extraction equipment to gather another by-product, methane gas, which Onyx plans to feed into generators that will supply electricity to the local grid. Finally, the waste is topped off with plastic caps, deodorised and landscaped, while a crystal-clear fountain at the entrance tinkles with the cleaned-up leachate.

The extremes represented by Shangba and Taihe explain why it is difficult to get an accurate picture of China's pollution. In a country where data are untrustworthy, corruption rife and the business climate for foreigners unpredictable, neither the cause of Shangba's problems nor the smooth efficiency of Taihe are necessarily what they seem. As with many other aspects of China's economic development, rapid progress and bold experiments in some areas are balanced by bureaucratic rigidity and stagnation in others.

Certainly, awareness of China's environmental problems is rising among policymakers at the highest level—reflected in a new package of right-sounding initiatives like a “green GDP” indicator to account for environmental costs. So is the pressure, both internal and international, to fix them. But while all developing economies face this issue, there are historical, political and institutional reasons why it will be a long and complicated process in China. There is some cause for optimism, not least an influx of foreign technology and capital. But progress on pollution is unlikely to be as rapid or uniform as the government and environmentalists desire.

Nor should it necessarily be. China's need to lift so many people out of poverty (the country's average annual income per head has only just breached $1,000), holds the edge over long-term considerations like sustainable development. The priorities of environmental activists, both foreign and Chinese, almost never reflect this. Greenpeace lobbies for China to invest in wind farms, an unrealistic answer to the country's power needs, while environmentalists from rich countries naively tell aspiring Chinese to eschew their new cars and air-conditioners.

Nor any drop to drink

That is not to deny the huge scale of China's environmental challenges. Water and waste pollution is the single most serious issue. Pan Yue, deputy head of the State Environmental Protection Administration (SEPA), the country's environmental watchdog ministry, calls it “the bottleneck constraining economic growth in China”. Per head, China's water resources are among the lowest in the world and concentrated in the south, so that the north and west experience regular droughts. Inadequate investments in supply and treatment infrastructure means that even where water is not scarce, it is rarely clean. Around half the population, or 600m people, have water supplies that are contaminated by animal and human waste.

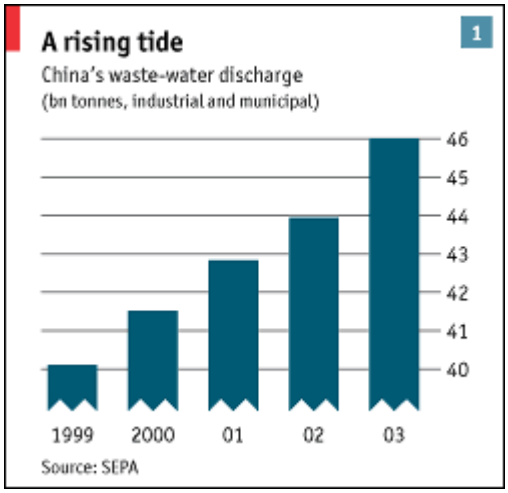
In late July an environmental disaster occurred on the Huai river, one of China's seven big rivers. A 133km-long black and brown plume swept along the river killing millions of fish and devastating wildlife. According to Mr Pan, the catastrophe occurred because too much water had been taken from the river system, reducing its ability to clean itself. Others say that numerous factories dump untreated waste directly into the water.

As for used water, with a national daily sewage rate of around 3.7 billion tonnes, China would need 10,000 waste-water treatment plants costing some $48 billion just to achieve a 50% treatment rate, according to Frost & Sullivan, a consultancy. SEPA found over 70% of the water in five of China's seven major river systems was unsuitable for human contact. As more people move into cities, the problem of household waste is becoming severe. Only 20% of China's 168m tonnes of solid waste per year is properly disposed of.

The air is not much better. “If I work in your Beijing, I would shorten my life at least five years,” Zhu Rongji told city officials when he was prime minister in 1999. According to the World Bank, China has 16 of the world's 20 most polluted cities. Estimates suggest that 300,000 people a year die prematurely from respiratory diseases.

The main reason is that around 70% of China's mushrooming energy needs are supplied by coal-fired power stations, compared with 50% in America. Combined with the still widespread use of coal burners to heat homes, China has the world's highest

emissions of sulphur dioxide and a quarter of the country endures acid rain. In 2002, SEPA found that the air quality in almost two-thirds of 300 cities it tested failed World Health Organisation standards—yet emissions from rocketing car ownership are only just becoming an issue. Hopes that China will “leapfrog” the West with super-green cars are naive, since dirty fuel messes up clean engines and the high cost of new cars keeps old ones on the road. Sun Jian, the second-ranking official at Shanghai's environmental protection bureau, estimates that 70% of Shanghai's 1m cars do not even reach the oldest European emission standards.



Farmland erosion and desertification resulted in Beijing being hit with 11 sandstorms in 2000, prompting Mr Zhu to wonder whether the advancing desert might force him to relocate the capital. A year later, the yellow dust clouds were so extensive that they raised complaints in South Korea and Japan and travelled as far as America. A partial logging ban and massive replanting appear to have reversed China's deforestation, but its grass and agricultural land continue to shrink.

Adding it all up, the World Bank concludes that pollution is costing China an annual 8-12% of its $1.4 trillion GDP in direct damage, such as the impact on crops of acid rain, medical bills, lost work from illness, money spent on disaster relief following floods and the implied costs of resource depletion. With health costs escalating (see article), that figure will increase, giving rise to some grim prognoses that growth itself will be undermined. “Ignored for decades, even centuries, China's environmental problems have the potential to bring the country to its knees economically,” argues Elizabeth Economy, author of “The River Runs Black”, a new book on China's pollution.

SEPA's Mr Pan is gloomier still: “Our natural resources will soon be unable to support our population.” His predecessor Qu Geping, the first head of China's National Environmental Protection Agency (SEPA's forerunner) in 1985, believes that while the official goal of quadrupling 2002 GDP by 2020 can be “healthily achieved”, if nothing is done about the environment, economic growth could grind to a halt.

But China's relationship with its environment has long been uneasy. For centuries, the country's rulers subjugated their surroundings rather than attempting to live in harmony with them. Mao declared that man must “conquer nature and thus attain freedom from nature”. In the past two decades, the toll extracted by China's manufacturing-led development and the sheer scale of its 9%-a-year economic expansion has only increased.

From conquest to nurture

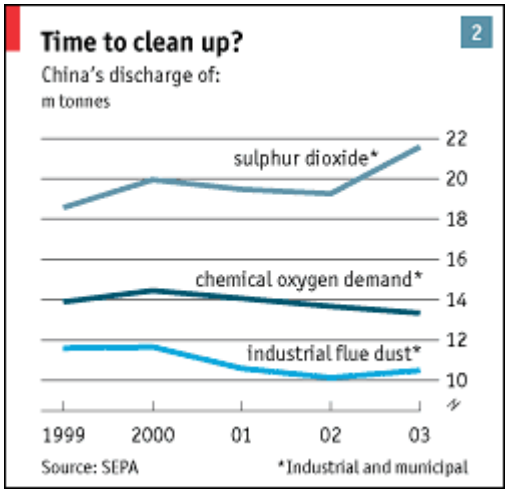
This has spurred the government into belated action. In 1998, Mr Zhu elevated SEPA to ministerial rank and three years later the 10th Five-year Plan for Environmental Protection set ambitious emission-reduction targets and boosted environmental spending to 700 billion yuan ($85 billion) for 2001-05—equivalent to 1.3% of GDP, up from 0.8% in the early 1990s (though still below the 2% suggested by the World Bank). A legal framework has been created. And the rhetoric has changed too, with Hu Jintao and Wen Jiabao, the current president and prime minister, now stressing balanced development rather than all-out economic growth.

Beijing's good intentions, however, have so far had only limited impact, thanks to the vast, decentralised bureaucracy through which it is forced to govern such a huge country. As Ken Lieberthal, a China expert at the University of Michigan, explains: “Much of the environmental energy generated at the national level dissipates as it diffuses through the multi-layered state structure, producing outcomes that have little concrete effect.”

SEPA, the government's chosen weapon in the fight against pollution, is under-resourced despite its enhanced status, with little money and just 300 central staff. In the capital, it must battle for influence with other agencies, such as the Construction Ministry that handles water and sewage treatment. Bureaucratic rivalries mean there is no co-operation and no sharing of the (often patchy) data that are collected with limited funds, observes Bruce Murray, the Asian Development Bank's representative in China.

Around the country, SEPA's branches, known as Environmental

Protection Bureaus, are supposed to monitor pollution, enforce standards and collect fines. But they are more in thrall to local governments—whose priorities are to maintain growth and employment in their jurisdiction—than to head office in Beijing. It is no rarity, therefore, to find a bureau imposing a fine on a dirty local enterprise (thus fulfilling its duty), but then passing the money on to the local administration, which refunds it to the company via a tax break. “The environmental management system needs real reform,” says Ma Jun, an environmental scholar. “The bureaus depend on the local government for their salaries and pensions. How can they enforce regulations against the local government?” Mr Pan complains that SEPA cannot effectively push through central edicts because it does not directly employ environmental personnel at the local level. Mr Sun at the Shanghai bureau says that SEPA has given him only 300 people with which to police 20,000 factories.



Make polluters pay

SEPA's impotence is one reason why penalties, even when it can impose them, remain laughably light. Mr Sun says the maximum he can fine a polluting company in Shanghai—a model city when it comes to the environment—is 100,000 yuan or about $12,000. But just as fundamental is that China lacks an understanding of the concept that the polluter should pay. “The legacy of the old, centrally planned economy is that electricity and water are treated as free goods or goods to be provided at minimal cost,” says the ADB's Mr Murray. Since the utilities cannot pass on the costs of cleaner water or lower power-station emissions to consumers, they fight any drive for higher standards and conservation tooth and nail. Even the central government is unwilling to impose price rises in basic services that could spark public unrest.

Water is an example. While customer tariffs have been raised in showcase cities, such as Beijing and Dalian in the north-east, water remains stunningly cheap in China. According to the World Bank, water for agriculture, which makes up three-quarters of the total used, is priced at 0.03 yuan (0.4 cents) per cubic metre, or about 40% of cost. More than half is lost in leaky irrigation systems. Meanwhile, the cost of more modern services, such as Guangzhou's solid-waste disposal, is entirely borne by the government.

Without the introduction of realistic pricing, China will not be able to afford to clean up its pollution, particularly the cost of enough foreign technology. Yet a system allocating the costs to the polluter will be hard to introduce and enforce. Even in Hong Kong, the territory's environment minister Sarah Liao concedes there is no tradition of having consumers bear the full costs of environmental regulations.

Ms Liao can also testify to the mainland's ambivalent attitude when it comes to letting outsiders help. She started looking into how the Pearl River delta's pollution was affecting Hong Kong back in 1999, but her requests to start monitoring emissions were repeatedly rebuffed even when she offered to pay for the equipment. Data collection finally started this year. For Thames Water, a British utility that is now a part of Germany's RWE, the experience was much worse. In June, Thames pulled out of a $73m advanced waste-water treatment plant it had built and was running in Shanghai, after the central government ruled that the fixed annual 15% return it had negotiated was now illegal.

There is no need to be unremittingly gloomy about China's environment, nevertheless. As developing countries get richer, they tend to pollute less. Nationally in China, discharges of chemical oxygen have declined over the past three years, those of industrial dust have stabilised and sulphur-dioxide emissions had been on the downtrend until 2003 when energy shortages increased demand for sulphurous coal (see charts). Most east-coast cities are enjoying more sunny days and the pollution load in the rivers is falling. Environmentally, in many places, China may have passed its nadir.

The government is increasing environmental spending and the more concerned attitude of the top leadership could filter down the hierarchy if the performance of officials starts being measured partly on environmental criteria, as Mr Qu hints it might. But the bigger incentive is that Beijing is under pressure to do more, partly from domestic public opinion. As urban Chinese see their material wealth increase, more are caring about the environment, while the concerns of the poor are increasingly being channelled by green non-governmental organisations. Though these remain extremely weak—few have more than a handful of members and all need government affiliation—Mr Wen said recently he suspended plans for

the construction of 13 dams along the Nu river in Yunnan province partly because of the concerns outlined by such groups.

External pressure is even greater. Despite reservations, foreign companies are flocking to China, scenting a fast-growing market for their environmental technologies and skills. International agencies are tying funds to environmental criteria, while foreign governments are beginning to complain about China's dust storms and greenhouse-gas emissions. All this will help spread best practices. Beijing is fast cleaning up ahead of the 2008 Olympics, moving out factories and introducing clean-vehicle technology: a new premium is being placed on global respectability.

Of course, environmental problems and their huge costs will dog China for many years. In a country where the public is not free to speak, too many courts are toothless and environmental groups remain on a tight leash, it will be hard to know if the government's avowedly green policies are being implemented. But China deserves credit for its attempts to clean itself up. The balance between sustainable development and economic growth will have to be continuously adjusted in the future. Right now, China is probably moving in the right direction.

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Oil

Unstoppable?

Aug 19th 2004 | NEW YORK
From The Economist print edition

Reuters

How OPEC's fear of $5 oil led to $50 oil

WHY are oil prices so high? That is a question to which the International Energy Agency, a quasi-governmental agency representing oil-consuming nations, would like an answer. Oil, as headlines have been screaming, this week reached a new record of $47. The agency's boffins are unimpressed. The title of the latest IEA report on oil, “Irrational Exuberance”, was a phrase made famous by Alan Greenspan, chairman of America's Federal Reserve, as he pondered the elevated levels of the stockmarket in 1996, albeit well before the share-price bubble burst.

There are in fact good and fundamental reasons for the recent rise. Demand for oil is soaring. Consumption appears to be growing at about 3% this year, up sharply from the level of recent years, thanks in part to robust petrol-guzzling in America, which consumes a quarter of the world's petroleum. The real surprise, however, has been China. Its booming economy has sucked up oil for use in everything from power generation to petrochemicals.

If demand is strong, supply has grown so uncertain that traders talk of a “risk premium” of perhaps $10 a barrel. In Russia, Vladimir Putin's murky assault on Yukos may lead to interruptions in exports. In Venezuela, Hugo Chávez, its president, survived a recall election last weekend but his opponents vow to fight on; last year, they shut down the oil sector completely. In Iraq, insurgents repeatedly disrupt exports. The greatest worry is that terrorists might damage the oil infrastructure in Saudi Arabia, the kingpin of OPEC and the only country with any spare capacity.

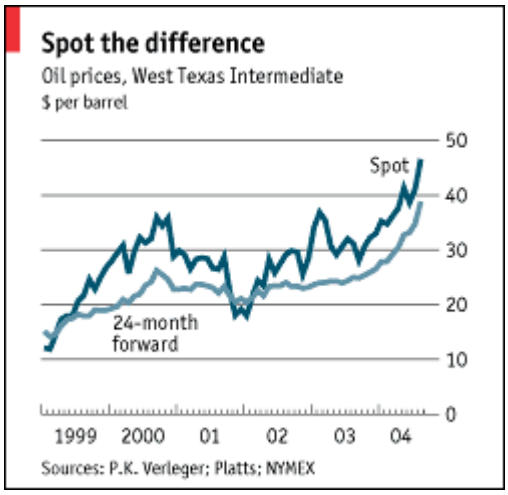
Other, less obvious factors have also pushed prices up. One is America's petrol market, where demand has been strong, but stocks low and supply constrained by environmental regulations and a lack of refining capacity. Pump prices have thus risen to levels that have Americans squealing. Philip Verleger, of the Institute for International Economics, argues that this tightness has had a knock-on effect on the price of crude oil everywhere because America is not only the world's biggest market, but also its most transparent.

Another powerful prop for oil prices may be the weak dollar, the currency in which oil is priced. OPEC complains that the recent fall in the dollar robs it of purchasing power (since its members buy things in

yen and euros as well). This irritation may have led the cartel to take a relaxed view about the recent rise in prices.

On the other hand, a weak dollar has been good for consuming countries in Asia. According to market gossip, Asian firms have been making big bets on oil for future delivery on the assumption that the dollar will remain weak. If oil prices rise while Asian currencies remain strong versus the dollar, these will prove lucrative.

Such bets may help explain the dramatic recent rise in the price of oil futures (contracts delivered months or years from now). Previous spikes in the price of oil for immediate delivery were not accompanied by a strong rise in the futures market (see chart), because consumers thought the spike was temporary.



Quite clearly, however, bets by Asian firms provide only part of the explanation, and a growing chorus argues that the rise in the forward price of oil means that consumers worldwide do not expect the oil price to fall below $30 for many years yet.

Punters, too, have been pushing up prices. Official data show that oil contracts held by hedge funds and other speculators hit an all-time high earlier this year. Though these positions have been cut in recent weeks, traders say that speculative interest remains strong. With interest rates low and stockmarket returns disappointing, betting on rising oil prices has proved highly lucrative. Such players might cut and run, however, should prices fall sharply, thus driving prices lower still.

The ghost of Jakarta

The biggest factor behind the extraordinary surge toward $50-a-barrel oil may well have been OPEC's fear of $5-a-barrel oil. On the eve of South-East Asia's financial crisis of the late 1990s, the cartel met in Jakarta and agreed to increase output. Alas, it misjudged the severity of the downturn. The result was a collapse in oil prices to $10 a barrel—a financial and political disaster for the cartel. Mr Chávez has said that if he and his OPEC colleagues had not cut production sharply, oil would have fallen to $5 a barrel.

Haunted by that memory, the Saudis pounced on the oil market with vigour. In the past few years, argues Mr Verleger, they have been propping up the oil price by keeping inventories down in consuming economies. By manipulating their production levels, he and other economists argue, the Saudis have ensured that firms in rich countries have had strong disincentives against holding stocks. That tightness inevitably buoyed oil prices.

Another factor related directly to the collapse in the oil price was OPEC's consequent reluctance to expand capacity. The cartel has not invested enough to keep pace with demand growth, so the world is virtually out of spare capacity. Growth in demand means that even Saudi Arabia no longer has enough to deal with two disruptions at once—as it did early last year when oil exports from both Venezuela and Iraq were knocked out.

So OPEC appears to have lost control of the oil market, for now at least. If demand cools, and especially if oil fields come online and restore the spare capacity of yesteryear, the cartel will regain its pricing power. In the meantime, the Saudis have little leverage. Ali Naimi, the Saudi oil minister, usually moves markets when he speaks. Yet when he promised a few days ago that more oil is on the way, traders ignored him and the rally continued apace.

The sceptics at the IEA may yet be proved right: oil prices could tumble at some point, especially if demand stops growing or declines. But as long as spare capacity remains so tight, high prices (and possibly even painful spikes) seem more likely. And even if prices do fall in coming weeks they may well stabilise at a higher level than in the 1990s.

Raymond Carbone, an oil trader on the New York Mercantile Exchange, assesses the supposed oil bubble this way: “This is not Nasdaq 1999. This bubble is not as fragile.” He then hastens to add, “unless there is a worldwide recession.” The irony is that the longer and stronger the current rally in oil prices, the greater the chance of such a downturn. That points to the best reason for OPEC to bring spare capacity

online as quickly as it can. When high oil prices push consuming economies into recession, it is the cartel itself that suffers most.

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South Korea

Stagflation returns

Aug 19th 2004 | TOKYO
From The Economist print edition

The country faces some nasty choices

Get article background

THE bad news is that the big economic menace of the 1970s has returned. The good news, for now at least, is that it has so far only afflicted South Korea and so far only in a mild form. With its economy already weak, South Korea has been hit by rising prices for oil. The effect has been to slow already meagre growth further and push up inflation. While the Bank of Korea, the central bank, tries to decide which is the bigger menace—its cut in interest rates on August 12th from 3.75% to 3.5% suggests that it is more concerned with growth—the country's other policy-makers have been flirting with policies that should have gone the way of platform boots: wage and price controls.

Consumer-price inflation has shot up recently, to 4.4% in the year to July, at the same time that growth has slowed. Although the economy grew by 5.3% in the first half of this year, that is slow by South Korean standards. It could slow much further. Domestic demand has been contracting, thanks partly to a hangover from a consumer-credit binge. The governor of the central bank, Park Seung, has warned that export growth could slow to single digits in the second half of this year, after rising 40% year-on-year in the first half. The central bank argues that core inflation (ie, not counting energy and food prices) remains manageable, and is likely to abate soon. It is more worried about growth.

But the government is clearly concerned about inflation. Among other steps, it has lowered charges for mobile phones—which just about everyone in South Korea seems to have—in hopes that this will weaken price rises. It is also considering steps to limit the profit margins of oil refiners. But while the latter might redistribute the burden of higher inflation, it will do nothing to alleviate the underlying inflationary pressures.

Dominique Dwor-Frecaut, an economist at Barclays Capital, reckons that the central bank made the right choice, given its limited options. South Korea's biggest problem, she argues, is an undervalued exchange rate. This benefits big exporters, such as the powerful family conglomerates known as *chaebol*, but at the expense of higher import prices, which punish smaller domestic firms and depress consumer spending.

The best solution, argues Ms Dwor-Frecaut, would be for South Korea to start running a fiscal deficit to increase demand, which it has been oddly reluctant to do. South Korean policymakers have begun putting together a stimulus package, albeit a mild one, which if passed could start to take effect by the middle of next year.

South Korea's problems are largely of its own making. Like their counterparts across Asia, South Korean policymakers have been obsessed with export-driven growth. Huge intervention over the past couple of years has been specifically designed to keep the won cheap and exports competitive. The byproduct has been higher inflation. Together with a fiscal stimulus, the government should therefore encourage the won to rise. It has lots of dollars to sell.

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China's economy

Dim sums

Aug 19th 2004
From The Economist print edition

China may have invented the abacus, but its statistics are dreadful

HOW rapidly is China's economy slowing? This question is key for assessing the chances of the country's red-hot economy achieving a soft landing rather than coming down to earth with a thud. Trouble is, Chinese economic statistics are notoriously unreliable. Until the late 1990s, the government sometimes published its quarterly GDP statistics before the quarter had even ended, which tells you something about their accuracy, or lack of it. The statistics may be getting a bit better, but the raw offical data is still not much help, especially for economists and investors trying to spot turning points.

One of the biggest problems is that China's official figures are not seasonally adjusted. That means resorting to year-on-year growth rates which, by definition, tend to be slow in picking up recent changes. In America and most other developed economies, by contrast, official data is seasonally adjusted, which allows analysts to compare month-on-month changes and quarter-on-quarter changes. In a desperate bid to throw more light on China's economy, many foreign investment banks have been trying to crunch their own seasonally adjusted numbers. These suggest an economy that is slowing much more rapidly than is indicated by official figures.

Take bank lending, which was growing at an annual pace of more than 20% last summer. The official figures show that the 12-month growth in lending slowed to 15.5% in July. However, Lehman Brothers estimates that, in the three months to July, growth at a seasonally adjusted annual rate slowed to only 10% compared with the previous three months. In other words, the measures aimed at cooling China's economy over the past year have worked.

The slowdown in industrial production looks even more dramatic. The 12-month rate of growth in China's industrial output slowed to a still-steaming 15.5% in July from 18% at the end of last year. However, Lehman's seasonally adjusted figures show output in the three months to July growing at an annual rate of less than 1% compared with the previous three months (see chart). Despite their seasonal adjustment, these numbers look too volatile, and thus may exaggerate the deceleration. But the economy has clearly slowed by more than the headline numbers suggest.

J.P. Morgan has seasonally adjusted China's GDP figures for some years. These show that growth slowed to an annual rate of only 2.3% in the second quarter from 10.6% in the first quarter. But the bank expects growth to bounce back to 7.5% in the current quarter.

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Mortgage banks

Double WaMu

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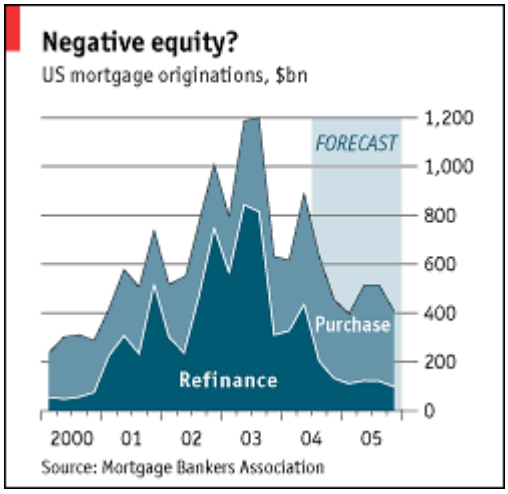
Big problems for a big mortgage bank

ALL good things must come to an end, a truth that Washington Mutual (WaMu), a mortgage-banking giant that transformed itself over seven years from a humble Seattle thrift to America's seventh-biggest bank by assets, is now discovering. After years of stellar growth, WaMu announced in late July that its second-quarter profits had halved compared with the same period in 2003. Though the bank blamed rising interest rates for its woes, its problems, all of them home-grown, run much deeper.

Like other mortgage banks, WaMu made huge profits from lending to American households eager to remortgage their homes at cheaper rates. But as interest rates have touched bottom, so the refinancing boom has turned to bust. Mortgage originations and refinancings have fallen sharply (see chart). So, naturally, have profits from this business.



But WaMu has suffered more than other banks because it is run badly. Its risk management is a mess. Mistakes in hedging the bank's servicing portfolio (which is supposed to make money from administering mortgages) generated a huge loss in the second quarter—causing WaMu's income from home mortgages to plummet from $531m in the first quarter of this year, to nothing in the second. Charlotte Chamberlain, an analyst at Jefferies & Company, an investment bank, points out that Countrywide, another mortgage bank, though one that hedges much of its (larger) servicing portfolio, did not experience any such problems. Nor did anybody else, for that matter. WaMu has hired BlackRock, another financial firm, to help it sort out its hedging.

A potentially bigger problem is WaMu's strategy. It grew rapidly over the past ten years by gobbling up a string of mortgage banks—a binge made possible by its fat profits from the refinancing boom. But in its rush to grow, the bank failed to pay enough attention to meshing its various back-office systems. The result has been a bloated cost structure that drags down profits when revenues from the bank's volatile mortgage operation fall.

Worse, says Kenneth Posner, an analyst at Morgan Stanley, it is unclear that big is necessarily better, even if WaMu had squeezed out efficiencies. “The mortgage business gets geometrically more complex with size,” he says. The lesson seems to have been lost on WaMu, which instead of getting rid of incompetent senior managers, has been trying to cut costs recently by firing masses of sales people and closing branches that sell mortgages. “This is backwards,” says Ms Chamberlain. “They are firing the people who generate assets instead of the managers at the top...a recipe for losing market share.”

Indeed, as WaMu retrenches, its two main competitors, Countrywide and Wells Fargo, are looking to expand aggressively. Wells Fargo, which already sells more mortgages than any other bank, wants to double its 10,000-strong sales force in the next few years. Countrywide, the second-biggest mortgage bank, is even treading on WaMu's toes: as part of its plan to triple its sales force by 2008, it plans to open perhaps a dozen new offices in Washington state.

Perhaps that will not worry WaMu too much, because WaMu wants to reduce exposure to the mortgage market and commercial lending, to concentrate instead on its consumer-banking business. The bank opened 66 retail branches in the second quarter of this year alone.

But relying on retail banking is hardly a safe bet. WaMu is far from alone in its penchant for bank branches and far from the first to spot their potential. Almost all of its competitors—from deep-pocketed behemoths such as Bank of America to nimble upstarts like Commerce Bank—have been doing the same for years. Some of the areas targeted by WaMu, such as Chicago, are fiercely competitive.

Nor does the bank seem to be very good at retail banking. CreditSights, a research firm, points out that the bank's deposit growth has been stagnant: deposits at its checking accounts grew only 1% in the second quarter compared with the year before, even though the bank has expanded hugely in the meantime.

And all this, note, even before the bank suffers any serious problems with defaults. Traditionally, Americans have taken out fixed-rate mortgages. But a growing proportion, many of them of dubious credit quality, have been lured by the seeming attractions of adjustable-rate mortgages, which now account for 40% of approvals. Borrowers' problems on these are likely to rise with interest rates. That means lenders would have troubles, too—including, one assumes, Washington Mutual: like other mortgage banks, most of the mortgages it now holds are of the adjustable-rate variety.

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Google's IPO

Playboys?

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Google's disappointing auction

SO MUCH for the hype. After months of anticipation, and days of delay by regulators, Google's initial public offering (IPO) was finally approved by America's Securities and Exchange Commission (SEC) on August 18th. But the company will get much less money than it had hoped. Instead of the stratospheric $108-135 a share it had expected, punters will be paying $85. At that price, the company will be worth about $23 billion, rather than the $35 billion or more that had seemed possible earlier. Moreover, the company will now sell fewer shares. The combined effect is to rake in less money—Google will get under $2 billion, rather than the hoped-for $3.5 billion.

What went wrong? Partly, it seems, investors have been put off by the complexities of the auction process. They are likely to have been troubled still more by the dismal performance of technology stocks of late. From Cisco to Hewlett-Packard, technology companies have taken to muttering about poor profits and sales in recent weeks. Nor has the lacklustre performance of the broader stockmarket, against an economy that is slowing, done much to provide a comforting backdrop.

But the company is also to blame for its woes. It has proved more than a little accident-prone, what with failing to register some shares that it had given to employees and contractors, and a row with Yahoo!, a competitor, over advertising technology. The most recent furore was over an interview that Larry Page and Sergey Brin, the company's founders, had given to *Playboy*. The interview was published in the “quiet period” mandated by the SEC.

Google's shares might, of course, still prosper. But its ambitious plans to curb the power of the big investment banks, who charge handsomely for taking a firm to market, are likely to have the opposite effect. Any boss worth his salt is likely to take one look at Google and head straight for Wall Street.

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Parmalat

The auditors' turn

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The bankrupt group's auditors are now in the firing line

Get article background

ENRICO BONDI, special administrator of the bankrupt Parmalat group, is a busy man. Only days after launching lawsuits against three banks—Citigroup, Deutsche Bank and UBS—involved in financial dealings with Parmalat before the massive fraud that caused the bankruptcy of the Italian food conglomerate was uncovered last December, he has now set off a new round of litigation. In the dock this time are Deloitte & Touche and Grant Thornton, two auditing firms that for years oversaw Parmalat's accounts. A lawsuit filed in Illinois on August 18th is seeking $10 billion in damages.

This is bad news for the auditors, who had been hoping that Parmalat's banks would continue to draw most of Mr Bondi's fire. For Deloitte the threat is that this affair becomes to it what Enron was to Arthur Andersen—a body-blow from which its reputation never recovers. The implications for Grant Thornton, a much smaller outfit that exists as a set of global affiliates, are less clear. Its non-Italian operations have already tried to distance themselves from the arm that drew up the accounts for key Parmalat subsidiaries.

Mr Bondi's strategy is clever. He has made all parties to lawsuits filed by Parmalat in America jointly liable for the $10 billion of damages he reckons are due. That way, even if he only wins one case he stands to recover impressive compensation for Parmalat's legitimate creditors. If he wins several cases, the defendants must divide the sum between them.

Last week, Mr Bondi published a formal list of those creditors, setting out his reasons for rejecting numerous claims by several of Parmalat's lead banks, chief among them Citigroup and Bank of America. If those rejections are upheld by a judge, the banks will not join the pool of creditors who stand to have their debt turned into shares. They will, in consequence, have no say in future votes about Parmalat's restructuring. Small wonder the banks are complaining that Mr Bondi's tactics are aggravating. He is doing well.

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Catastrophe insurance

Weathering well

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Insurers thrive, thanks to government support

THE biggest hurricane since Hurricane Andrew in 1992 seems to have left the insurers battered but not blown away. Hurricane Andrew cost the insurance industry $15.5 billion, sent some smaller companies to the wall, and led to a surge in premiums on property insurance. Estimates for the costs for Charley, which swept through Florida on August 13th, are still being calculated, but they look to be about $7 billion or so, according to the Insurance Information Institute. None of the big insurers seem threatened; indeed their shares rose. Allstate, the second-biggest insurer of Florida homes, expects no "material impact" on its financial stability.

Insurers have a love-hate view of disasters. On the one hand, they may have to settle big claims. But they also drive up premiums, making business more profitable. For now, premiums on commercial property are just shy of a 12-year peak. Any hopes that Charley will push them higher still are likely to be disappointed, however, such is the big role that the government now plays in insuring huge risks.

As well as causing a spike in premiums, Andrew brought in a host of new insurers, mainly based in Bermuda. But the state now also takes more of the pain than it once did. The biggest insurer against hurricane damage in Florida is Citizens Property Insurance Corporation, which is state run. So is the Florida Hurricane Catastrophe Fund (FHCF), set up in 1993. This is funded by premiums from insurers doing business in Florida. In turn it provides them with reinsurance if claims go above $4.5 billion, up to a maximum of $15 billion. Since Florida has been blessedly disaster-free, the fund is flush with cash.

Not everyone is happy that government is playing such a big role in Florida. Some in the insurance industry grumble that the government is edging out private reinsurers. But most are relieved that the state is becoming more heavily involved. The California Earthquake Authority, which like the Florida fund is publicly managed, has hoarded more than $7 billion in case of the next Big One.

Then there is terrorism insurance. After September 11th, Congress passed the Terrorism Risk Insurance Act, which made the government a backstop for huge claims. But the act expires at the end of next year. Panicked because they will begin writing policies for 2005 this September, insurers are begging lawmakers to extend it.

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Economics focus

Realistic rewards

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The return on equities over the next decade is likely to be much lower than most investors expect

AFTER rebounding strongly in 2003, America's S&P 500, the benchmark index for American stockmarkets, has fallen by 8% since its high earlier this year. America's battle-hardened investors seem to think of this as little more than a flesh wound. Surveys suggest that they still expect average annual returns from equities of at least 10% over the next decade; many, indeed, have based their retirement plans on this assumption. Alas, they are likely to be severely disappointed.

That might seem strange. After all, these expectations are far lower than at the peak of the bubble in 2000, after five wild years had delivered annual average returns of 25% and investors expected more of the same. They also look fairly conservative compared with the annual return of 13% that stocks delivered during the 45 years to 1995, before the bubble inflated. However, a study by Martin Barnes, an economist at the Bank Credit Analyst, a Canadian research firm, concludes that, at best, the average return over the next ten years is likely to be half that over the past half century.

His sobering forecast is based on two assumptions, both very reasonable. The first is that, because of lower inflation, company profits are unlikely to rise by more than 5% a year over the next decade, a bit slower than the average of 7% a year over the past 50 years. In the long run, profits tend to grow in line with GDP, and America's nominal GDP is thought likely to grow by around 5% a year over the next decade (3% real growth plus 2% inflation). Although profits have outpaced GDP over the past couple of years, this is unlikely to continue because pre-tax profit margins are nearly at their highest in 35 years. And since firms now operate in a world of greater competition, profit margins are, if anything, more likely to fall than to rise.

Mr Barnes's second assumption is that there is little scope for a sustained rise in the valuation of shares. The S&P 500 is currently trading at around 18 times historic operating profits. That is far below its ratio of almost 30 at the peak of the bubble, but still higher than its 50-year average of 15. Mr Barnes's "optimistic" scenario assumes that the p/e ratio stays flat over the next decade as a whole and the S&P 500 rises in line with profit growth of 5% a year. Adding in dividends, this would give an average annual return of 6.7%. That implies an average real return of only 4.7%, compared with almost 10% in the half century to 2000. However, history suggests that there is a risk that the p/e ratio could fall over the next

decade. In an alternative scenario, Mr Barnes assumes that the p/e ratio reverts to its historic average of 15. If so, the annual return would be a measly 4.7%.

Investors have become used to much higher returns than the range of 4.7-6.7% suggested as likely by Mr Barnes because their expectations are still coloured by the 18% average annual return of the bull market from 1982 to 2000. But those two decades of falling inflation and falling interest rates provided an exceptional, probably unique, boost to equities. The present era of low and stable inflation is good for economic growth. It is unlikely to be good, however, for financial markets or, indeed, those that rely on them for their living.

Belt tightening

Lower equity returns have serious implications for financial-services firms and consumers. The bloated financial sector will need to go on a diet. Two decades of above-average returns from shares and bonds (thanks also to falling inflation), and hence a big increase in the public's appetite for investing in shares, caused a huge expansion in the financial-services industry. Employment in the financial sector and its share of GDP more than doubled between the early 1980s and 2000 and have fallen only slightly since. More extraordinary still has been the surge in the financial sector's share of total stockmarket capitalisation, from 6% in 1980 to 23% this year.

Lower financial returns will mean slower growth in commissions and investment-management fees. Over the past two decades, as markets have been liberalised, financial firms have relied less on commissions and more on trading revenues. But these will be harder to come by in a world of low returns. That is why many banks are now gearing up their returns with more borrowed money. But when this latest strategy comes unstuck because of the greater volatility which the strategy itself will eventually cause in financial markets, banks and fund managers will be under pressure to shrink.

Far more worrying, of course, is what lower returns mean for consumers. Underfunded pension schemes hoping for another bull market in shares to fill the gap are likely to be severely disappointed. And because companies' profits will be squeezed as employers are thus forced to make bigger contributions to pension funds, the death knell for defined-benefit pension schemes cannot be that far off.

Partly for the same reason, those that rely on their own investments are unlikely to fare better. Anybody who has based retirement plans on the assumption that equities will do as well in the future as they have done in the past is in trouble. Big gains in share prices boosted household wealth and caused a large drop in saving over the past two decades. Why save much if booming shares did the job for you? Since this particular get-rich-quick scheme lost some of its allure after 2000, households have shifted their affections to property, the price of which has taken over where stockmarkets left off. Surveys suggest that home-buyers also expect double-digit returns over the next decade. Alas, this is very unlikely: house prices in many cities are already at record highs compared with incomes and rents.

If actual returns on assets turn out much lower than expected, households will be forced to save more and spend less to meet their retirement goals. Mr Barnes hopes that household saving will rise gradually over several years. This would present only a gradual headwind to economic growth. The risk, of course, is that saving rises much more quickly.

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Gravitational anomalies

An invisible hand?

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An unexplained effect during solar eclipses casts doubt on General Relativity

“ASSUME nothing” is a good motto in science. Even the humble pendulum may spring a surprise on you. In 1954 Maurice Allais, a French economist who would go on to win, in 1988, the Nobel prize in his subject, decided to observe and record the movements of a pendulum over a period of 30 days. Coincidentally, one of his observations took place during a solar eclipse. When the moon passed in front of the sun, the pendulum unexpectedly started moving a bit faster than it should have done.

Since that first observation, the “Allais effect”, as it is now called, has confounded physicists. If the effect is real, it could indicate a hitherto unperceived flaw in General Relativity—the current explanation of how gravity works.

That would be a bombshell—and an ironic one, since it was observations taken during a solar eclipse (of the way that light is bent when it passes close to the sun) which established General Relativity in the first place. So attempts to duplicate Dr Allais's observation are important. However, they have had mixed success, leading sceptics to question whether there was anything to be explained. Now Chris Duif, a researcher at the Delft University of Technology, in the Netherlands, has reviewed the evidence. According to a paper he has just posted on arXiv.org, an online publication archive, the effect is real, unexplained, and could be linked to another anomaly involving a pair of American spacecraft.

Three different types of instrument have been used to detect the Allais effect. The first are conventional pendulums, such as the one Dr Allais used originally. The second are torsion pendulums, which work by hanging a bar that has weights at each end from a wire. As the wire twists back and forth, the bar rotates in pendulum-like motion. The third are gravimeters, which are, in essence, very precise scales. All of these instruments measure the acceleration due to gravity at the Earth's surface, a quantity known as *g*. The Allais effect is a small additional acceleration, so tiny that it would take an apple about a day to fall from a tree branch if it were the only gravitational effect around.

Allez, Allais

Dr Duif has examined various conventional explanations for the Allais effect. He finds the most obvious suggestion—that it is a mere measuring error—unlikely, because similar results have been found by many different groups, operating independently and, in at least one case, without knowledge of Dr Allais's results.

He also discounts several explanations that rely on conventional physical changes that might take place during an eclipse. One of these is that the anomaly is caused by the seismic disturbance induced as crowds of sightseers move into and out of a place where an eclipse is visible. That seems unlikely, given that one of the experiments with a positive result was conducted in a remote area of China while another that had a negative result took place in Belgium, one of the most crowded parts of the planet. Dr Duif also considered the possibility that, because the moon's shadow cools the air during an eclipse, this cooler, and thus denser, air might exert a different gravitational pull on the instruments. This change could, he reckons, affect a gravimeter, but it cannot account for the results from the pendulums.

Dr Duif rules out a third explanation, too: that cooling of the Earth's crust due to the eclipse shadow causes the ground to tilt slightly, and thus distorts the results. He notes that although a detectable tilt is caused when the temperature drops by a few degrees, that tilt is too small to explain the anomalies and, in any case, it would lag roughly 30 minutes behind the shadow (because it takes time for the ground to cool) while the experimental measurements show a change in *g* instantaneously during an eclipse.

Although Dr Duif discounts each of the conventional explanations on its own, he admits that they might, in combination, account for the Allais effect. But the possibility also remains that General Relativity—Einstein's sacred child—is wrong.

This suggestion would fit in with another odd phenomenon: the fact that the *Pioneer 10* and *11* space-probes, launched by NASA, America's space agency, in the early 1970s, are receding from the sun slightly more slowly than they should be.

According to a painstakingly detailed study by the Jet Propulsion Laboratory, the part of NASA responsible for the craft, there is no conventional explanation for this. There may, of course, be no relationship with the Allais effect. But Dr Duif points out that the anomalous force felt by both *Pioneer* probes (which are travelling in opposite directions from the sun) is about the same size as that measured by some gravimeters during solar eclipses.

So what are the alternatives? One possibility (though it could not account for the *Pioneer* observations) is known as Majorana shielding. This eponymous theory is that large masses (such as the moon) partially block the gravitational force from more distant objects (such as the sun). Another idea is “MOND”, or Modified Newtonian Dynamics, a theory put forward in 1983 by Moti Milgrom of the Weizmann Institute in Israel. MOND suggests that at very low accelerations gravity gets a bit stronger. An even stranger suggestion, made in 2002 by Mikhail Gershteyn, then at the Massachusetts Institute of Technology, is that the force of gravity is different in different directions. Most physicists do not like that one at all. It requires that the conceptual “frames of reference” against which movement, acceleration and so on are measured, are not uniform in all directions. But it was a similarly radical idea—that there is no absolute frame of reference in the universe, only local frames that can be measured relative to one another, which put the “relativity” into relativity theory in the first place...

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Sudden infant-death syndrome

Foredoomed or forewarned?

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Cot deaths are caused, in part, by genes

DOES sudden infant-death syndrome (SIDS), or “cot death”, run in families? That question is both medically significant (for establishing which children are most at risk, and advising parents accordingly) and legally significant (since if it does, it would provide an alternative explanation to serial infanticide in cases where more than one baby in a family has died). It may also be sociologically significant since, in America at least, SIDS is more common in African-descended children than in European-descended ones—a fact that the prejudiced might be inclined to lay at the door of the parents.

Work published in September's issue of *Pediatric Research*, by Debra Weese-Mayer, of Rush University in Chicago, and her colleagues, suggests that a predisposition to SIDS may, indeed, be inherited. Dr Weese-Mayer has found a link between SIDS and mutations of several genes involved in the construction and function of the autonomic nervous system. This part of the nervous system controls many organs and muscles, including those involved in breathing. Mutations affecting it might easily cause infantile death.

Dr Weese-Mayer's team identified several sections of DNA that are harbouring autonomic-nervous-system-related genes. They sequenced these sections from the chromosomes of 92 babies who had died of SIDS, and compared the results with those from the same chromosomal regions in 92 control babies who had passed their first birthdays (SIDS generally strikes in the first year of life) and who had no family history of diseases of the autonomic nervous system. The study found 11 different autonomic-nervous-system-related mutations in 14 of the SIDS babies, but only one such mutation in two of the controls. Of the SIDS babies who had at least one mutation, 71% were classified as “black”.

If confirmed by further research, this will be an important result. SIDS claims some 2,300 babies a year in America. In Britain, the figure is around 300. Clearly, bad genes are not the only factor. Other risks include the baby's sleeping position. Campaigns such as “Back to Sleep”, which urged parents to put babies to sleep on their backs, led to a 75% fall in SIDS cases between 1986 and 1998 in Britain. In America, similar campaigns have led to similar decreases. But establishing a genetic component to SIDS—and showing which genes are involved—will help to show how the risks interact.

It will also help defendants. In Britain, Trupti Patel was accused of multiple murder after three of her babies died. Sir Roy Meadow, a consultant paediatrician who has been involved in a number of cot-death cases, told the court categorically that “sudden, unexpected death does not run in families”. Mrs Patel's grandmother begged to differ. She told the court that she had suffered five similar deaths, and Mrs Patel was acquitted.

Because of the Patel case and others like it, Sir Roy is being investigated for serious professional misconduct by the General Medical Council, the governing body of Britain's doctors. The country's attorney-general, Lord Goldsmith, has so far reviewed more than 100 cases similar to Mrs Patel's, but announced earlier this year that only a few will be referred to the Court of Appeal. Perhaps Dr Weese-Mayer's evidence will persuade him to look again.

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Linguistics

Language barriers

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Can a concept exist without words to describe it?

TAKE heart, those of you who struggled with maths at school. It seems that words for exact numbers do not exist in all languages. And if someone has no word for a number, he may have no notion of what that number means.

The Pirahã, a group of hunter-gatherers who live along the banks of the Maici River in Brazil, use a system of counting called “one-two-many”. In this, the word for “one” translates to “roughly one” (similar to “one or two” in English), the word for “two” means “a slightly larger amount than one” (similar to “a few” in English), and the word for “many” means “a much larger amount”. In a paper just published in *Science*, Peter Gordon of Columbia University uses his study of the Pirahã and their counting system to try to answer a tricky linguistic question.

This question was posed by Benjamin Lee Whorf in the 1930s. Whorf studied Hopi, an Amerindian language very different from the Eurasian languages that had hitherto been the subject of academic linguistics. His work led him to suggest that language not only influences thought but, more strongly, that it determines thought.

While there is no dispute that language influences what people think about, evidence suggesting it determines thought is inconclusive. For example, in 1972, Eleanor Rosch and Karl Heider investigated the colour-naming abilities of the Dani people of Indonesia. The Dani have words for only two colours: black and white. But Dr Rosch and Dr Heider found that, even so, Dani could distinguish and comprehend other colours. That does not support the deterministic version of the Whorf hypothesis.

While recognising that there are such things as colours for which you have no name is certainly a cognitive leap, it may not be a good test of Whorf's ideas. Colours, after all, are out there everywhere. Numbers, by contrast, are abstract, so may be a better test. Dr Gordon therefore spent a month with the Pirahã and elicited the help of seven of them to see how far their grasp of numbers extended.

Using objects with which the participants were familiar (sticks, nuts and—perhaps surprisingly—small batteries), he asked his subjects to perform a variety of tasks designed to measure their ability to count. Most of these tests involved the participant matching the number and layout of a group of objects that Dr Gordon had arranged on a table.

The tests began simply, with a row of, say, seven evenly spaced batteries. Gradually, they got more complicated. The more complicated tests included tasks such as matching numbers of unevenly spaced objects, replicating the number of objects from memory, and copying a number of straight lines from a drawing.

In the tests that involved matching the number and layout of objects they could see, participants were pretty good when faced with two or three items, but found it harder to cope as the number of items rose. Once it was beyond eight, they were getting it right only three-quarters of the time. The only exception was in those tests that used unevenly spaced objects—an arrangement that can be perceived as a group of clusters. Here, performance fell off when the number of objects was six, but shot up again when it was between seven and ten. Dr Gordon suggests that the participants used a “chunking” strategy, counting the clusters and the numbers of objects within each cluster separately.

Things were worse when the participants had to remember the number of objects in a layout and replicate it “blind”, rather than matching a layout they could see. In this case the success rate dropped to zero when the number of items became, in terms of their language, “many”. And line drawing produced

the worst results of all—though that could have had as much to do with the fact that drawing is not part of Pirahã culture as it did with the difficulties of numerical abstraction. Indeed, Dr Gordon described the task of reproducing straight lines as being accomplished only with “heavy sighs and groans”.

The Pirahã are a people who have steadfastly resisted assimilation into mainstream Brazilian culture. Their commerce takes the form of barter, with no need to exchange money. Exact numbers do not exist in their language simply because there is no need for them. And in this case, what you do not need, you do not have. At least in the field of maths, it seems, Whorf was right.

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Lobsters in Maine

Claws!

Aug 19th 2004 | NORTH HAVEN, MAINE
From The Economist print edition

Have Maine's lobsters become plentiful through judgment or luck?

AP

Big enough to live?

ANYONE aboard a lobster boat “hauling in” off the coast of Maine will observe the frequency with which the captain heaves a trap on to the rails, opens it and then throws the lobsters back into the water. The process looks like a rare brand of insanity to the uninitiated, but actually represents a carefully calibrated system of natural-resource management. Lobstermen chuck overboard any female lobster bearing eggs, any lobster shorter than a minimum size, and also any “jumbo” larger than an agreed maximum.

The “eggers” are released to create the next generation of lobsters and the tiddlers to grow and mate—both common strategies in fisheries management. The jumbos, however, are released because experiments carried out in aquaria suggest that male size is sexually selected, indicating that big males (which females much prefer to mate with) have the best genes. Big females, on the other hand, are particularly valuable breeders because they produce many more eggs than small ones.

On top of this, there is evidence from other types of fishery that removing the biggest individuals from a population affects the gene pool in a way that results in the evolution of a smaller maximum size, which is not what the customer wants at all. So, even though those in the know admit that some captains will scrape a female's eggs from her tail and keep her illegally, the rules appear, for the most part, to be observed.

Those rules were introduced in the mid-1990s under a system of “co-management” in which government scientists set goals for the state's lobster population and lobstermen then decide how to reach them. As the rules were put in place, the lobster population in Maine's waters began a sharp upward climb—the 2003 season saw 24.7m kg (54.5m lb) of lobsters landed in Maine's docks, a haul more than two and a half times the 1945-85 average, and one worth approximately $200m. Even though the number of lobster traps has increased from 2m in 1990 to 3m today, the consensus is that not only has the size of the catch increased, but the size of the underlying population has as well. It looks like a fabulous success for marine management. But is it?

Some ecologists suspect that the explosion of the lobster population in Maine may be due not only to the regulations, but also to the fact that the Gulf of Maine represents an ecosystem out of balance. In a recent paper in *Ecosystems*, Robert Steneck and his colleagues at the University of Maine report that 4,500 years of archaeological data from village middens along the coast, and also more recent fishing records, suggest that fishing pressures may have pushed the ecosystem of the Gulf of Maine into a new, less-stable state. For thousands of years, cod and other bottom-feeding fish were the top predators in the system. However, overfishing throughout the past century has so depleted these populations that they no longer fulfil this role. The study suggests that the lobster explosion is as much a consequence of this as of better management.

The explanation goes like this. Bottom-feeders prey on young lobsters, but they also prey on sea urchins. As their numbers declined in the 1980s, those of the urchins rose. Sea urchins graze the kelp that lobsters use as cover, so the initial drop in bottom-feeders did not benefit lobsters since although they had fewer predators, they were more exposed. Meanwhile, the sea-urchin population increased steeply until its discovery by the Japanese sushi industry led to heavy harvesting and a subsequent crash in the early 1990s. Between 1992 and 2002, the sea-urchin catch fell by 63%. The kelp cover returned, but the

bottom feeders continued to be overfished (Maine's cod catch plummeted by 70% during the decade), so the lobster population shot up. The result is a glut of the young adult lobsters useful to commercial fishermen, which co-management probably helps to maintain, but which might prove unstable in the long run.

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About sponsorship

Business books

How 51 Gorillas Can Make You Seriously Rich

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Or, why so many business books are awful

IF YOU want to profit from your pen, first write a bestselling business book. In few other literary genres are the spin-offs so lucrative. If you speak well enough to make a conference of dozing middle managers sit up, your fortune is made. You can, says Mark French of Leading Authorities, a top speaking agency, make a seven-figure income from speechifying alone.

Given this strong motivation to succeed, it is astonishing how bad most business books are. Many appear to be little more than expanded PowerPoint presentations, with bullet points and sidebars setting out unrelated examples or unconnected thoughts. Some read like an extended paragraph from a consultant's report (and, indeed, many consultancies encourage their stars to write books around a single idea and lots of examples from the clientele). Few business books are written by a single author; lots require a whole support team of researchers. And all too many have meaningless diagrams.

The formula seems to be: keep the sentences short, the wisdom homespun and the typography aggressive; offer lots of anecdotes, relevant or not; and put an animal in the title—gorillas, fish and purple cows are in vogue this year. Or copy Stephen Covey (author of the hugely successful “Seven Habits of Highly Effective People”) and include a number. Here, though, inflation is setting in: this autumn sees the publication of “The 18 Immutable Laws of Corporate Reputation” by Ronald Alsop. And Michael Feiner has written a book offering “the 50 basic laws that will make people want to perform better for you”.

The fundamental problem is that a successful business book needs a bright idea, and they, in the nature of business, come along infrequently. The dotcom boom brought some, the spurs to Clayton Christensen's “The Innovator's Dilemma” or Rosabeth Moss Kanter's “Evolve!” (accompanied by a CD of the guru herself rapping her message). Since then, new books have tended to focus on three areas: corporate governance; leadership; and how to make money out of bits of the business that were forgotten in the boom.

The first category has produced the most meticulous work, with books such as “The Recurrent Crisis in Corporate Governance” by Paul MacAvoy, an academic, and Ira Millstein, a lawyer. Inevitably, many books have raked over the lessons of Enron, WorldCom and other failures, trying to explain what went wrong.

Some of the leadership books are written (or ghost-written) by the likes of Rudy Giuliani or Jack Welch, to describe the secrets of their success. Others explain the mysterious qualities that successful leaders display. Warren Bennis's “Geeks & Geezers”, for example, compares different formative experiences on the way to the top. Of course, the most perceptive leadership literature was written 400 years ago by William Shakespeare; and some of today's most readable books discuss the techniques of past heroes, such as Alexander the Great. They will teach you history, even if they do not make you Jack Welch.

The sheer number of business books means that the diamonds shine rarely in a mound of dross. Counting everything from property management to personal finance, there are perhaps 3,000 business titles published each year in the United States, easily the largest market. One industry insider estimates, on the basis of figures from Nielsen Bookscan and a hunch about Amazon's sales, which Bookscan excludes, that a total of 8m-10m books that could broadly be defined as “business” are sold in America each year. They are almost all written by North Americans: Charles Handy, the Irish author of “The Age of Unreason”, is one of the few non-Americans who has managed to break into this market.

Including Amazon's figures, the top 50 business books sold around 4m copies in the first seven months of this year. But many sell fewer than 1,000 in their first year, and the fall-off in sales is almost always dramatic. “The shelf-life of maximum relevance is measured in months,” says Adrian Zackheim, who made his name publishing Jim Collins's “Good to Great”, one of the rare business books that has topped bestseller lists for years.

It is hard to believe that many managers run their businesses differently as a result of their reading. Occasionally, however, a truly great business book will articulate an idea that helps them to explain what it is that they are trying to do. It creates phrases—such as “core competence” or “emotional intelligence”—that fit the moment. But a few lines of “Henry IV, Part II” might well serve the same function, and give more pleasure too.

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About sponsorship

Alexander McCall Smith

A ladies' detective man

Aug 19th 2004 | GABORONE
From The Economist print edition

A new woman in the life of Precious Ramotswe's creator

CHORTLING from under his Panama hat, Alexander McCall Smith admits feeling daunted by his sudden celebrity. Five years ago he was an obscure Edinburgh author with a cult following: today, the creator of "The No. 1 Ladies' Detective Agency" is one of the most popular writers alive. He frets that he will get big-headed after receiving fan mail from African presidents, occupants of the White House and famous fellow writers. Effusive praise at a reception in Gaborone, Botswana's capital, recently moved him to tears.

He is best known for the gentle adventures of Precious Ramotswe, Botswana's answer to Agatha Christie's Miss Marple: an honest woman of "traditional build" with a fondness for bush-tea, amiable conversation and sleuthing. Nearly 5m copies of the first five books about her have been bought in English in the past five years. Editions in Bulgarian, Icelandic, Slovene and some 30 other languages sell well too.

You can expect to see more of the genial Ms Ramotswe. A sixth book, "In the Company of Cheerful Ladies", has just been published in Britain, and at least two more are planned. Then the good lady is to appear on screen. The Miramax film-production company and Anthony Minghella (director, inter alia, of "The English Patient") are to make at least three Ms Ramotswe television films.

That is all spawning interest in Mr McCall Smith's considerable backlist. "I stopped counting how many I had written after the 50th book," he says airily. He is especially fond of his three-volume "Portuguese Irregular Verbs", which is not a grammar book but a collection of short tales poking fun at eccentric Germans. Later this year he will begin a novel to be serialised in the *Scotsman*, following the success of "44 Scotland Street", published daily over six months earlier this year.

Readers like his direct style and the feel-good nature of his stories: endings are usually happy, and few characters are outright evil. The darkest are more often vain, self-important or inconsiderate. Mr McCall Smith bristles at the suggestion that he writes for children. Adults are engaged by the moral dilemmas that he portrays; especially appealing are Ms Ramotswe's integrity and care for others. These traits are typical of the parts of Africa that Mr McCall Smith knows well, where he says "there is a profound decency in people who have moral time for each other."

His characters' troubles are mostly mundane, not the wars and disasters that dominate much news from the continent. While not romanticising Africa—AIDS kills one person close to Ms Ramotswe—he feels "a need to write with courtesy" about it. Botswana, at least, may be benefiting. Tourist arrivals there have soared in the past four years, even as his books have become popular. Many now tour Gaborone in search of "Speedy Motors" garage and other spots described in the books.

As a moral philosopher, Mr McCall Smith wants his books to have both good consequences and big sales (the latter have paid for a custard-coloured Mercedes). At 55 he has just become a full-time fiction writer, having given up a legal-academic career and vacated chairs on bio-ethics committees in Britain and for UNESCO. But the novelist still dabbles in ethics. The first book of a new series, "The Sunday Philosophy Club", will be published next month. It stars a Scottish lady detective, Isabel Dalhousie, who unravels crimes and ethical conundrums at the same time, a sort of Mrs MacRamotswe.

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The social art of Wen Zhengming

Aug 19th 2004
From The Economist print edition

AP

This illustration, from “Elegant Debts” by Craig Clunas, a professor at London's School of Oriental and African Studies, is by the man described as the Michelangelo of Chinese art. One of the masters of the Ming era, Wen Zhengming (1470-1559) was a contemporary of the Italian (1475-1564). But the wellspring of his art was very different. Most of his works, exquisite composites of poetry, calligraphy and painting, were done to repay obligations. The magnolia branch shown here was attached to a thank-you note. Mr Clunas shows Wen's art to have been part of the “messy nature of obligations” in Chinese society, not a European-style outpouring of a tormented soul. His book opens western readers' eyes to a refreshingly different framework for thinking about artistic genius.

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About sponsorship

Reason and religion

No room for moderation

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From The Economist print edition

THIS book will strike a chord with anyone who has ever pondered the irrationality of religious faith and its cruel and murderous consequences—from the Spanish Inquisition to the suicide bombs of devout young Islamists. After noting that a majority of the world's population still believes in some kind of divine creator, Sam Harris goes on to show how one holy book after another promises paradise to believers and damnation to all others. Deuteronomy tells believers to have no mercy on apostates ("You must stone him to death, since he has tried to divert you from Yahweh, your God"); death is the punishment for anyone breaking the Ten Commandments; and "those that deny Our revelations shall be punished for their misdeeds," says the Koran.

Against such a background, argues Mr Harris, "moderation" is a self-deluding "myth" which "springs from the fact that even the least educated person among us simply knows more about certain matters than anyone did 2,000 years ago—and much of this knowledge is incompatible with scripture." In other words, religious moderates (who are surely the vast majority of the faithful) are forced constantly to reinterpret supposedly immutable revelations of the truth in an attempt to reconcile their faith with their reason.

The End of Faith: Religion, Terror, and the Future of Reason
By Sam Harris

To be published in Britain by Free Press in February 2005.
Norton; 256 pages; $24.95.

Buy it at Amazon.com

Many people would think that a good thing, since moderation implies tolerance and respect for other faiths. Mr Harris disagrees: tolerance on the part of moderates is precisely the attitude that allows extremists to flourish. "By failing to live by the letter of the texts, while tolerating the irrationality of those who do," he says, "religious moderates betray faith and reason equally." And therefore, goes the argument, they connive in all the horrors carried out in the name of their imagined creator. Only when we renounce the impossible paraphernalia of religion—for example, the virgin birth (attested to by only two of the apostles) or the ascension of Muhammad to heaven—will reason be free to rescue mankind from religious terrorism that tries to send all non-believers to hell and only the faithful to heaven.

It is a clever thesis by a clever man (Mr Harris has a philosophy degree from Stanford and is completing a doctorate in neuroscience). In the context of the author's homeland, much more religiously inclined than Europe, it is also a controversial one: Mr Harris quotes Gallup poll findings that 35% of Americans believe "the Bible is the literal and inerrant word of the Creator of the universe", and "another 48% believe that it is the 'inspired' word of the same—still inerrant, though certain of its passages must be interpreted symbolically before their truth can be brought to light."

But is the argument ultimately convincing? Presumably not to true believers, though even Mr Harris's critics will have to concede the force of an analysis which roams so far and wide, from the persecution of the Cathars to the composition of George Bush's cabinet.

By contrast, Mr Harris's supporters may be disappointed by his efforts to reconcile spirituality—"a natural propensity of the human mind"—with reason and ethics. His approval of eastern philosophy and Buddhism is much too brief to be helpful, and it is hard to grasp the assurance that, "Mysticism is a rational enterprise. Religion is not." But never mind: the reader can turn to 62 pages of references and closely argued notes for further enlightenment.

The End of Faith: Religion, Terror, and the Future of Reason.
By Sam Harris.
Norton; 256 pages; $24.95.

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About sponsorship

New fiction

Unhappy families

Aug 19th 2004
From The Economist print edition

FAMILIES “have idealised expectations of each other,” writes Justin Cartwright in this accomplished new novel exploring the fragility of family life in times of crisis. “On the one hand more allowances are made, but also more is demanded.” Such allowances and demands are at the heart of the Judd family—parents and three grown-up children—as they reel from the shock of the elder daughter's conviction for art theft and her two-year sentence in an American prison.

The book starts at the time of Juliet's release and focuses on the emotions each member of the family faces as they prepare for her homecoming to England. Each feels they bear some responsibility for her downfall, but this affects them in strikingly different ways.

To appease her sense of maternal failure, Daphne, Juliet's mother, sinks herself into the distracting ephemera of organising a wedding that she hopes will be the family's salvation. But it is her father, Charles, who suffers most. His inability to cope with his beloved daughter's fate causes him to feel as if “his soul had thinned to nothing”. He is filled with a raging impotence, angry that the hopes he once had for Juliet have come to such an end.

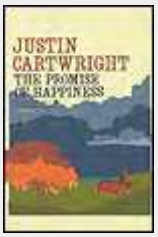
Mr Cartwright, who won a Whitbread award in 1998 for “Leading the Cheers”, a portrayal of small-town America, is a perceptive narrator of familial desperation. He invokes vivid images with simple, clean sentences and, despite the underlying seriousness of the book, injects his prose with a refreshing layer of humour that provides a counter to the weighty themes of guilt and redemption.

While all the Judd family members are well rounded, their personalities and attitudes skilfully drawn, background characters too come to life through the use of a finely turned phrase or two. Customers in an American diner, for example, wear baseball caps “at a rural angle”. A waitress is from “the battered-old-broad school of waitressing”.

One of the most compelling aspects of the novel is the way the author avoids favouring any one character over another. The book is written from the perspective of a wise observer, and the reader is given a balanced and ultimately heart-warming portrayal of a family struggling to cope with the disintegration of established certainties. It is a funny, moving and powerful story, and deserves wide acclaim.

The Promise of Happiness.
By Justin Cartwright.
Bloomsbury; 306 pages; £16.99

The Promise of Happiness
By Justin Cartwright



Bloomsbury; 306 pages; £16.99

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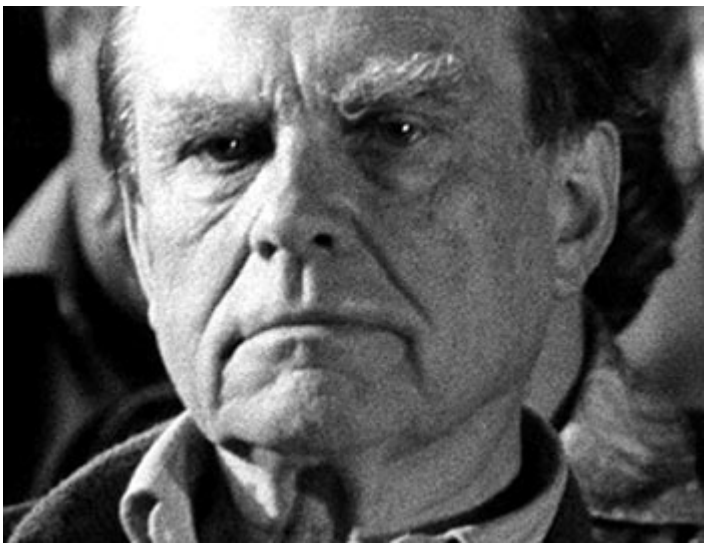
About sponsorship

Obituary

Czeslaw Milosz

Aug 19th 2004
From The Economist print edition

AP



Czeslaw Milosz, a Polish émigré poet, died on August 14th, aged 93

HE WAS a poet who spanned his century. Born in a Lithuanian-Polish province of tsarist Russia, Czeslaw Milosz died having seen the Nazi and Soviet totalitarian empires rise and fall, while his two native lands finally escaped their miserable history to end up safe and free. He wrote about it all, mostly in exile in America, in essays, novels and volumes of poems. These lines of his are inscribed on a monument at the Gdansk shipyard, honouring Polish workers shot for striking against the dictatorship of the proletariat:

> Do not feel safe. The poet remembers.
>
> You can kill one, but another is born.
>
> The words are written down, the deed, the date.

In retrospect, the Communists and their goons who banned his poems should have been scared. History has proved Mr Milosz right about pretty much everything. But at the time, and particularly until he won the Nobel prize for literature in 1980, it was a long slog.

> When will that shore appear from which at last we see
>
> How all this came to pass and for what reason?

he asked sadly in 1974 in “From the Rising of the Sun”, a poem that his friend and fellow-émigré, the Russian Joseph Brodsky, considered his best.

His greatness was often against the spirit of the age, largely because the ages in which he lived had so many nasty spirits. He was liberal-minded, xenophile, wistful and tolerant, in a world that was none of these things. That made him, in his words, “an ecstatic pessimist”. Feeling gloomy, he cheerfully got on with writing.

In pre-war Poland Mr Milosz felt stifled by the prevailing Catholic-nationalist ethos; he was sacked from a

Polish radio station for being too pro-Lithuanian. Under Nazi occupation, he worked with the resistance, among other things translating “The Waste Land” into Polish for an underground publisher. Before it showed its truly Stalinist face, he served the post-war regime as a diplomat; in 1951, he defected.

For the next 40 years he tried to explain to the West both the real nature of Communism, and the things it had extinguished. Mr Milosz liked to describe himself as the last citizen of the Grand Duchy of Lithuania, a medieval superpower that stretched from the Baltic to the Black Sea, noted for its religious and cultural tolerance. But that, and its surviving echoes in the modern era, had disappeared like Atlantis. Mr Milosz's erudite nostalgia for the ethnographical intricacies of the eastern Polish provinces, the “border of Rome and Byzantium” as he put it, seemed fanciful and archaic. Now, as the European Union wonders how best to deal with its sullen, poverty-stricken eastern neighbours, his thoughts on culture and history could hardly be more topical.

In his best-known prose work, “The Captive Mind”, Mr Milosz caught not only the nastiness of totalitarian ideology, but also its seductiveness. An intellectual who swallows the Communist medicine of the mind, he wrote, “attains a relative degree of harmony...preferable to the torment of pointless rebellion and groundless hope.”

His poems dealt with metaphysics, immortality, love, memory and beauty. A masterful observer of sights and sounds, he used small details from his youth to illustrate large ideas. That, he said, was a Proustian “search for reality purified by the passage of time”, as in the opening stanzas of “Earth”, written in 1949:

> My sweet European homeland,
>
> A butterfly lighting on your flowers stains its wings with blood,
>
> Blood gathers in the mouths of tulips,
>
> Shines, star-like, inside a morning glory
>
> And washes the grains of wheat.
>
> Your people warm their hands
>
> At the funeral candle of a primrose
>
> And hear on the fields the wind howling
>
> In the cannons ready to be fired.
>
> You are a land where it's no shame to suffer
>
> For one is served here a glass of bitter liquor
>
> With lees, the poison of centuries.

Writing in Polish is not the easiest way to become world-famous, and it was only in 1973 that a volume of his poetry appeared in English. His recognition was aided by excellent translators, principally Richard Hass, an American poet laureate and a professor, like Mr Milosz, at Berkeley.

The intellectual tussles of the cold war were tricky too. Diehard anti-Communists distrusted him for having served the regime at all. America at first refused to give him a visa, leaving him stranded and cash-strapped in Paris, where he was befriended by Albert Camus. Other intellectuals found his critique of totalitarianism too harsh. Pablo Neruda denounced him in a left-wing newspaper as “The man who ran away”.

That charge hurt: Mr Milosz was always worried that he had betrayed his homeland by leaving it and was glad to return to newly free Poland for the final years of his life. He was welcomed as a literary giant. But like many east European intellectuals who flourished in adversity, he had little to say directly about the new era of uncaptive minds. “Intellectuals have a certain image of things and don't know very well what is going on beneath, in people's heads, after those decades of totalitarian smashing and modelling,” he said. His many fans thought that too modest.

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Overview

Aug 19th 2004
From The Economist print edition

Oil prices continued to climb, even after worries about the result of Venezuela's presidential referendum subsided. West Texas Intermediate, a variety traded on American exchanges, rose to more than $47 a barrel, as traders fretted over the global oil supply.

Trade figures from **America** delivered a mixed message. The goods and services trade deficit widened sharply in June to $55.8 billion, up from $46.9 billion in May. Exports fell by 4.3% while higher oil prices pushed up the value of imports by 3.3%. But there was some good news: America's Treasury Department said that net foreign purchases of American securities rose strongly between May and June, suggesting that foreigners are still willing to finance Americans' spending.

Despite foreigners' confidence, **American consumers** may be losing faith. The University of Michigan's consumer-confidence index fell to 94.0 in early August from 96.7 in July.

Inflation in America remains mild. Consumer prices grew by 3.0% in the year to July, down from 3.3% in the year to June. Core inflation, which excludes the volatile prices of food and energy, ran at 1.8% in the year to July, down from 1.9% in the year to June. **Industrial production** grew by 0.4% in July, a weaker-than-expected performance, and by 4.9% in the year to July.

Housing starts in America shot up by 8.3% in July, reversing a decline of 7.7% in June.

Japan's economy grew much more slowly than expected in the second quarter, plunging to a 1.7% annual rate, thanks partly to lower business investment. GDP grew at an annual rate of 6.6% in the first quarter.

The **euro area's** economic growth was also disappointing in the second quarter. GDP grew by 0.5%, for an annual rate of 2.0%, which was slightly below the consensus forecast. Industrial production rose by 2.7% in the year to June, down from growth of 3.7% in the year to May. **Germany's** ZEW confidence index fell in August to its lowest level since July 2003, as worries about oil prices took their toll.

In **Sweden**, industrial output slowed to 3.4% in the year to June.

Producer prices in **Switzerland** fell by 0.1% in the month of July, but rose by 1.3% in the 12 months to July.

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Output, demand and jobs

Aug 19th 2004
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2004	2005	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 3.2	Q1	+ 0.9	+ 3.5	+ 3.3	– 1.1	Q1	+ 7.9	Q2	5.7	Jul	6.2
Austria	+ 0.5	Q1	+ 0.8	+ 1.6	+ 2.1	+ 6.6	May	– 4.7	May	4.2	Jul	4.5
Belgium	+ 2.8	Q2	+ 3.2	+ 2.2	+ 2.1	+ 2.7	Jun	– 2.5	May	12.8	Jul†	13.0
Britain	+ 3.7	Q2	+ 3.8	+ 3.3	+ 2.7	+ 0.5	Jun	+ 6.6	Jul	4.8	Jun††	5.0
Canada	+ 1.6	Q1	+ 2.4	+ 2.9	+ 3.4	+ 3.6	May	+ 4.9	Mar	7.2	Jul	7.7
Denmark	+ 1.4	Q1	+ 3.8	+ 2.0	+ 2.2	+ 3.9	Jun	+ 4.3	Jun	6.4	Jun	6.3
France	+ 2.8	Q2	+ 3.2	+ 2.2	+ 2.2	+ 2.7	Jun	+ 4.1	Jun	9.9	Jun	9.8
Germany	+ 1.5	Q2	+ 1.9	+ 1.5	+ 1.7	+ 2.2	Jun	– 2.2	Jun	10.6	Jul§	10.6
Italy	+ 1.1	Q2	+ 1.0	+ 1.2	+ 1.8	– 0.1	Jun	– 5.3	May	8.5	Jan	8.9
Japan	+ 4.4	Q2	+ 1.7	+ 4.5	+ 2.3	+ 8.9	Jun	– 2.9	Jun	4.6	Jun	5.3
Netherlands	+ 1.0	Q2	– 0.8	+ 1.3	+ 1.8	nil	Jun	– 1.0	May‡	6.3	Jul**	5.3
Spain	+ 2.8	Q1	+ 2.6	+ 2.8	+ 2.8	+ 5.7	Jun	+ 2.1	Jun	11.1	Jun	11.3
Sweden	+ 3.4	Q2	+ 3.8	+ 2.8	+ 2.6	+ 3.4	Jun	+ 4.3	Jun	5.8	Jun†	4.8
Switzerland	+ 1.5	Q1	+ 1.6	+ 1.9	+ 2.1	+ 4.5	Q1	+ 6.2	Jun	3.6	Jul†	3.6
United States	+ 4.8	Q2	+ 3.0	+ 4.5	+ 3.5	+ 4.9	Jul	+ 5.6	Jun	5.5	Jul	6.2
Euro area	+ 2.0	Q2	+ 2.0	+ 1.8	+ 2.0	+ 2.7	Jun	+ 1.2	Jun	9.0	Jun	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.7	Q1	+ 3.0	na	na	+ 5.2	Jun	+ 3.4	Jun	8.9	Jun†	9.6
Greece	+ 3.9	Q2	– 0.6	na	na	– 1.5	Jun	+ 4.0	May	na		na
Iceland	+ 4.9	Q1	na	na	na	na		na		3.1	Jun†	3.2
Ireland	+ 6.1	Q1	na	na	na	+ 4.2	Jun	+ 5.4	May	4.4	Jul	4.8
Luxembourg	+ 2.1	2003	na	na	na	– 1.2	Dec	+ 2.3	Mar	3.9	Jun	3.5
New Zealand	+ 4.4	Q1	+ 8.1	na	na	+ 5.5	Q1	+ 6.8	Q2	4.0	Q2	4.7
Norway	+ 2.9	Q1	+ 3.9	na	na	+10.4	Jun	+ 5.3	Jun	4.6	Q2	4.7
Portugal	+ 0.1	Q1	+ 2.4	na	na	– 0.2	Jun	+ 5.2	Jun	6.3	Q2†	6.1

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ‡New series. ††Apr-Jun; claimant count rate 2.7% in Jul. §EU harmonised rate 9.9% in Jul. **May-Jul.

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Prices and wages

Aug 19th 2004
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% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2004	2005	latest		year ago	latest		year ago
Australia	+ 2.5	Q2	+ 2.7	+ 2.5	+ 2.5	+ 2.8	Q2	+ 0.2	+ 5.1	Q1	+ 4.4
Austria	+ 2.3	Jul	+ 1.1	+ 1.6	+ 1.5	+ 6.0	Jul	+ 1.2	+ 2.2	Jun	+ 2.1
Belgium	+ 2.4	Jul	+ 1.5	+ 1.8	+ 1.6	+ 4.2	Jun	– 0.8	+ 2.3	Apr	+ 1.7
Britain	+ 1.4	Jul*	+ 1.3	+ 1.5	+ 1.8	+ 2.5	Jul	+ 1.3	+ 4.4	Jun†	+ 3.0
Canada	+ 2.5	Jun	+ 2.6	+ 2.0	+ 2.1	+ 6.4	Jun	– 2.7	+ 2.6	May	+ 3.0
Denmark	+ 1.3	Jul	+ 1.9	+ 1.3	+ 1.9	+ 2.7	Jul	– 0.1	+ 3.3	Q1	+ 3.9
France	+ 2.3	Jul	+ 1.9	+ 2.1	+ 1.7	+ 2.2	Jun	+ 0.9	+ 2.8	Q1	+ 2.9
Germany	+ 1.8	Jul	+ 0.9	+ 1.6	+ 1.2	+ 3.9	Jul	nil	+ 1.8	May	+ 1.4
Italy	+ 2.3	Jul	+ 2.7	+ 2.3	+ 2.1	+ 3.2	Jun	+ 1.5	+ 3.3	Jun	+ 1.7
Japan	nil	Jun	– 0.4	– 0.1	+ 0.3	+ 1.6	Jul	– 0.8	+ 0.8	Jun	+ 4.0
Netherlands	+ 1.1	Jul	+ 2.1	+ 1.5	+ 1.4	+ 3.7	Jun	+ 1.2	+ 1.2	Jul	+ 2.6
Spain	+ 3.4	Jul	+ 2.8	+ 2.8	+ 2.6	+ 4.0	Jun	+ 0.9	+ 3.2	Q1	+ 4.9
Sweden	+ 0.7	Jul	+ 1.8	+ 0.8	+ 1.6	+ 1.5	Jun	– 1.6	+ 2.0	May	+ 2.6
Switzerland	+ 0.9	Jul	+ 0.2	+ 0.7	+ 1.1	+ 1.3	Jul	– 0.7	+ 1.4	2003	+ 1.8
United States	+ 3.0	Jul	+ 2.1	+ 2.6	+ 2.3	+ 4.0	Jul	+ 2.9	+ 1.9	Jul	+ 2.9
Euro area	+ 2.3	Jul	+ 1.9	+ 2.0	+ 1.7	+ 2.4	Jun	+ 1.4	+ 2.5	Q1	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.3	Jul	+ 0.4	na	na	+ 1.5	Jul	– 0.4	+ 3.5	Q2	+ 4.4
Greece	+ 2.9	Jul	+ 3.6	na	na	+ 1.9	Jun	+ 3.1	na		na
Iceland	+ 3.7	Aug	+ 2.0	na	na	+ 5.2	Jul	+ 3.3	+ 5.1	Jun	+ 5.6
Ireland	+ 2.7	Jul	+ 3.1	na	na	+ 1.3	Jun	–10.6	+ 6.1	Q4	+ 6.4
Luxembourg	+ 2.4	Jul	+ 1.6	na	na	+ 7.7	May	+ 2.7	– 0.4	Dec	+ 0.7
New Zealand	+ 2.4	Q2	+ 1.5	na	na	– 0.6	Q1	– 1.3	+ 2.3	Q2	+ 2.3
Norway	+ 1.5	Jul	+ 1.5	na	na	+13.6	Jul	+ 6.3	+ 4.6	Q1	+ 5.3
Portugal	+ 2.8	Jul	+ 2.9	na	na	+ 2.4	Jun	+ 0.8	+ 1.3	May	– 1.9

*New series. RPI inflation rate 3.0% in Jul. †Apr-Jun.

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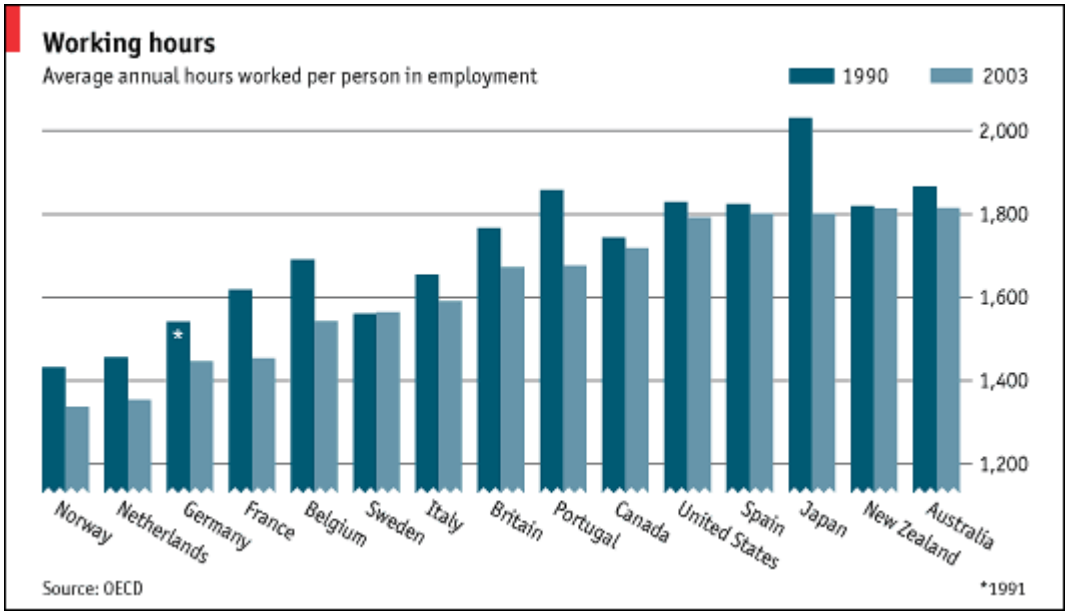
Working hours

Aug 19th 2004
From The Economist print edition



The average number of hours worked per year has been falling in most rich countries over the past decade. Some European countries are now trying to reverse the trend, but they have a long way to go. In 2003, the French and Portuguese worked 10% fewer hours than in 1990; Germans worked 6% fewer than in 1991. The number of hours of labour per worker has fallen even more steeply in Japan, by 11% in 1990-2003.

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Money and interest rates

Aug 19th 2004
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Aug 18th 2004)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 4.4	+11.8	Jun	5.42	4.83	5.17	5.58	5.46	6.37
Britain	+ 5.6	+ 8.9	Jul	4.91	3.44	4.84	4.95	4.56	5.71
Canada	+15.6	+ 8.1	Jun	2.05	2.76	2.99	4.68	4.82	6.16
Denmark	+ 7.7	+ 9.1	Jun	2.25	2.30	2.38	4.17	4.33	5.40
Japan	+ 4.0	+ 1.9	Jul	0.03	0.01	0.13	1.58	1.42	1.71
Sweden	+ 2.6	+ 0.8	Jun	1.98	2.72	2.67	4.32	4.70	2.75
Switzerland	+ 3.8	+ 3.0	Jul	0.52	0.25	0.98	2.63	2.62	2.37
United States	+ 4.0	+ 4.8	Jul	1.64	1.05	2.41	4.22	4.35	5.75
Euro area†	+ 9.6	+ 5.4	Jun	2.11	2.14	2.41	4.04	4.13	3.83

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 5.04%, Japan No. 262 1.565%. Central bank rates: US fed funds 1.50%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.75%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Aug 19th 2004
From The Economist print edition

1995=100

	Aug 10th	Aug 17th*	% change on one month	% change on one year
Dollar index				
All items	89.1	89.2	– 4.1	+13.9
Food	82.8	82.4	– 6.2	+ 6.2
Industrials				
All	97.6	98.4	– 1.5	+24.0
Nfa†	91.9	90.4	– 2.2	+ 9.2
Metals	102.5	105.3	– 0.9	+37.5
Sterling index				
All items	76.4	77.0	– 2.7	– 1.3
Euro index				
All items	95.2	95.2	– 3.7	+ 2.4
Yen index				
All items	105.1	104.5	– 2.6	+ 4.9
Gold				
$ per oz	399.95	403.25	+ 0.9	+11.8
West Texas Intermediate				
$ per barrel	44.49	46.77	+15.8	+52.1

* Provisional. † Non-food agriculturals.

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Stockmarkets

Aug 19th 2004
From The Economist print edition

Market indices

	Aug 18th	2004 high	2004 low	% change on one week	% change on record high	% change on Dec 31st 2003 in local currency	% change on Dec 31st 2003 in $ terms
Australia (All Ordinaries)	3,488.6	3,565.3	3,274.9	– 0.9	– 2.2	+ 5.5	nil
Austria (ATX)	2,042.7	2,047.0	1,568.9	+ 2.7	– 0.2	+32.2	+28.9
Belgium (Bel 20)	2,477.2	2,517.3	2,244.2	+ 0.6	–32.7	+10.4	+ 7.6
Britain (FTSE 100)	4,355.3	4,575.7	4,287.0	+ 1.0	–37.2	– 2.7	– 1.0
Canada (Toronto Composite)	8,223.0	8,898.8	8,123.5	+ 0.7	–27.8	nil	– 1.2
Denmark (KBX)	238.2	241.3	219.0	+ 1.0	–21.1	+11.5	+ 8.9
France (SBF 250)	2,423.2	2,594.4	2,386.1	+ 1.1	–44.8	+ 0.5	– 2.0
(CAC 40)	3,541.5	3,811.4	3,465.3	+ 1.1	–48.8	– 0.5	– 3.0
Germany (DAX)	3,726.5	4,151.8	3,647.0	+ 1.3	–53.8	– 6.0	– 8.4
Italy (BCI)	1,256.5	1,340.3	1,239.5	+ 0.7	–42.4	nil	– 2.5
Japan (Nikkei 225)	10,774.3	12,163.9	10,365.4	– 2.5	–72.3	+ 0.9	– 1.4
(Topix)	1,094.9	1,217.9	1,022.6	– 2.3	–62.0	+ 4.9	+ 2.5
Netherlands (AEX)	316.7	364.8	310.7	+ 1.2	–54.9	– 6.2	– 8.6
Spain (Madrid SE)	816.1	881.7	804.4	+ 1.1	–28.8	+ 1.0	– 1.5
Sweden (Affarsvarlden Gen)	196.0	218.1	188.5	+ 1.3	–51.0	+ 4.1	– 0.2
Switzerland (Swiss Market)	5,325.2	5,934.4	5,309.8	– 0.8	–36.7	– 3.0	– 4.0
United States (DJIA)	10,083.1	10,737.7	9,814.6	+ 1.5	–14.0	– 3.5	– 3.5
(S&P 500)	1,095.2	1,157.8	1,063.2	+ 1.8	–28.3	– 1.5	– 1.5
(NASDAQ Comp)	1,831.4	2,153.8	1,752.5	+ 2.7	–63.7	– 8.6	– 8.6
Europe (FTSE Eurotop 300)*	951.9	1,026.2	940.9	+ 0.6	–44.2	– 0.6	– 3.1
Euro area (FTSE Ebloc 100)*	800.5	888.3	787.2	+ 1.1	–48.4	– 3.7	– 6.2
World (MSCI)†	1,018.0	1,085.8	997.0	+ 1.3	–29.7	– 1.8	– 1.8
World bond market (Citigroup)‡	606.5	619.5	575.1	+ 1.0	– 2.1	+ 0.5	+ 0.5

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms.
‡Citigroup World Government Bond Index, total return, in $ terms.

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About sponsorship

Trade, exchange rates and budgets

Aug 19th 2004
From The Economist print edition

	Trade balance*, $bn latest 12 months	Current account $bn latest 12 mths	Current account The Economist poll % of GDP, forecast 2004	Current account The Economist poll % of GDP, forecast 2005	Exchange rate trade-weighted† 1990=100 Aug 18th	Exchange rate trade-weighted† 1990=100 year ago	Currency units per $ Aug 18th	Currency units per $ year ago	Currency units per £	Currency units per euro	Currency units per ¥100	Budget balance % of GDP 2004‡
Australia	− 16.9 Jun	− 33.0 Q1	− 5.4	− 3.9	84.2	83.6	1.40	1.51	2.55	1.72	1.28	0.5
Austria	− 0.1 May	− 2.0 May	− 0.4	− 0.2	102.8§	103.1	0.81	0.90	1.48	–	0.74	-1.3
Belgium	+ 20.8 Jun	+ 12.2 Mar	+ 3.5	+ 3.4	102.9§	103.3	0.81	0.90	1.48	–	0.74	-0.2
Britain	− 93.6 Jun	− 39.2 Q1	− 2.4	− 2.0	104.6	99.1	0.55	0.63	–	0.67	0.50	-2.9
Canada	+ 50.0 Jun	+ 20.9 Q1	+ 2.2	+ 1.6	88.1	83.6	1.31	1.40	2.39	1.61	1.19	1.2
Denmark	+ 10.2 Jun	+ 7.1 Jun	+ 2.7	+ 2.6	106.6	106.2	6.05	6.68	11.0	7.44	5.52	0.9
France	+ 3.7 Jun	+ 2.5 May	+ 0.7	+ 0.8	106.3§	106.8	0.81	0.90	1.48	–	0.74	-3.8
Germany	+186.4 Jun	+ 93.7 Jun	+ 2.8	+ 2.6	104.0§	104.5	0.81	0.90	1.48	–	0.74	-3.7
Italy	+ 3.4 May	− 14.5 Jun	− 1.0	− 0.8	75.9§	76.1	0.81	0.90	1.48	–	0.74	-3.1
Japan	+128.9 Jun	+163.6 Jun	+ 3.5	+ 3.6	133.8	130.2	110	118	200	135	–	-7.1
Netherlands	+ 33.5 Jun	+ 20.7 Q2	+ 2.8	+ 2.8	102.4§	102.8	0.81	0.90	1.48	–	0.74	-3.1
Spain	− 60.1 May	− 30.0 May	− 2.9	− 2.6	77.0§	77.4	0.81	0.90	1.48	–	0.74	0.3
Sweden	+ 22.6 Jun	+ 21.2 Q1	+ 6.4	+ 5.8	80.5	79.6	7.51	8.31	13.7	9.23	6.85	0.2
Switzerland	+ 7.7 Jun	+ 37.5 Q4	+10.5	+10.2	113.0	111.6	1.25	1.39	2.28	1.54	1.14	-1.6
United States	−589.5 Jun	−537.3 Q1	− 5.2	− 4.4	96.3	105.1	–	–	1.82	1.23	0.91	-4.7
Euro area	+107.6 May	+ 58.4 May	+ 0.5	+ 0.6	90.9	89.2	0.81	0.90	1.48	–	0.74	-2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 14.5 Jun	+ 10.6 Jun	na	na	81.9§	82.2	0.81	0.90	1.48	–	0.74	1.6
Greece	− 27.5 May	− 9.3 Jun	na	na	59.5§	59.7	0.81	0.90	1.48	–	0.74	-3.2
Iceland	− 0.4 Jun	− 0.7 Q1	na	na	95.2**	98.2	71.1	80.4	130	87.4	64.8	0.2
Ireland	+ 41.8 May	− 2.1 Q1	na	na	93.9§	95.2	0.81	0.90	1.48	–	0.74	-0.5
Luxembourg	− 3.9 May	+ 3.2 Q1	na	na	102.9§	103.3	0.81	0.90	1.48	–	0.74	-1.8
New Zealand	− 2.2 Jun	− 3.4 Q1	na	na	105.7	100.7	1.51	1.70	2.75	1.85	1.37	2.9
Norway	+ 30.1 Jul	+ 29.4 May	na	na	97.0	96.7	6.76	7.45	12.3	8.31	6.17	10.4
Portugal	− 15.8 May	− 8.8 May	na	na	93.3**	92.9	0.81	0.90	1.48	–	0.74	-3.8

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, June average. ‡OECD forecast. **IMF, April average.

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About sponsorship

Exchange-rate forecasts

Aug 19th 2004
From The Economist print edition

Exchange-rate forecasts

From J.P. Morgan Chase, currency units per $

	August 18th	3-month	12-month
Euro area*	1.23	1.23	1.22
Japan	110	104	102
Australia	1.39	1.37	1.35
Britain†	1.82	1.84	1.79
Canada	1.31	1.30	1.32
Denmark	6.05	6.05	6.09
Sweden	7.50	7.34	7.46
Switzerland	1.25	1.22	1.20
China	8.28	8.20	7.80
Singapore	1.71	1.68	1.65
South Korea	1,158	1,100	1,120
Brazil	2.99	3.08	3.15
Mexico	11.3	11.6	11.6
Poland	3.62	3.60	3.50
Russia	29.2	29.0	29.0
South Africa	6.52	6.30	6.75

*$ per € †$ per £

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Overview

Aug 19th 2004
From The Economist print edition

South Africa's central bank unexpectedly cut its key interest rate by one-half of a percentage point to 7.5%, causing the rand to fall sharply. **Hungary's** central bank also cut interest rates by half a point, to 11%, another move that defied expectations.

Peru's economy is slowing. GDP growth fell to 3.0% in the year to June, down from 4.0% in the year to May.

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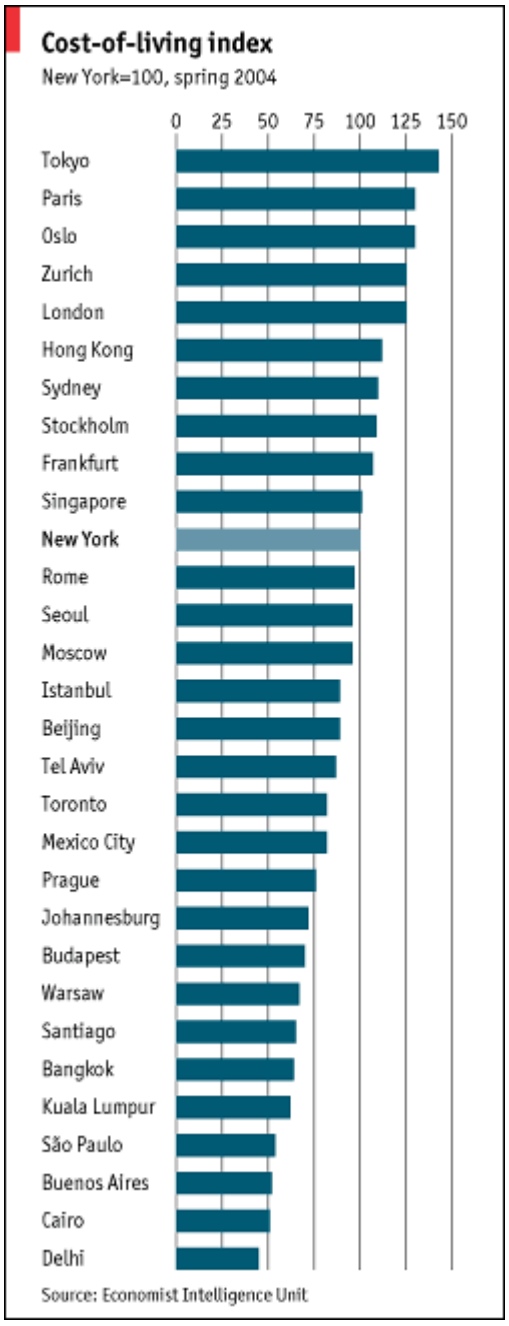
Cost-of-living index

Aug 19th 2004
From The Economist print edition

Tokyo remains the world's most expensive city, but Paris is now close behind, according to a dollar-based survey of 133 cities by the Economist Intelligence Unit, a sister company of *The Economist*. Paris's rising cost is mostly due to the strong euro. American cities, by contrast, seem cheaper thanks to a weak dollar. For much the same reason, life in Sydney has become 10% dearer in dollar terms than in New York.



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Economy

Aug 19th 2004
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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.6	Q2	+15.5	Jul	+ 5.3	Jul	+15.7	Jul	+45.9	2003	470.6	Jun
Hong Kong	+ 6.8	Q1	+ 1.8	Q1	– 0.1	Jun	–13.0	Jun	+14.3	Q1	118.3	Jul
India	+ 8.2	Q1	+ 7.3	Jun	+ 3.0	Jun	–17.1	Jun	+ 8.7	Q1	113.0	Jul
Indonesia	+ 4.3	Q2	+24.0	May	+ 7.2	Jul	+27.9	Jun	+ 7.4	Q4	33.7	Jun
Malaysia	+ 7.6	Q1	+13.3	Jun	+ 1.3	Jul	+19.5	Jun	+13.0	Q1	54.3	Jul
Philippines	+ 6.4	Q1	– 1.6	May	+ 6.0	Jul	– 1.5	Jun	+ 3.9	Mar	12.8	Jul
Singapore	+12.5	Q2	+19.4	Jun	+ 2.3	Jun	+15.7	Jul	+27.6	Q1	100.3	Jul
South Korea	+ 5.3	Q1	+12.3	Jun	+ 4.4	Jul	+30.0	Jul	+24.6	Jun	167.0	Jun
Taiwan	+ 6.3	Q1	+15.7	Jun	+ 3.3	Jul	+12.7	Jul	+27.4	Q1	230.4	Jul
Thailand	+ 6.5	Q1	+ 9.4	Jun	+ 3.1	Jul	+ 1.7	Jun	+ 7.0	Jun	42.3	Jun
Argentina	+10.7	Q1	+ 9.5	Jun	+ 4.9	Jul	+13.4	Jun	+ 6.1	Q1	18.1	Jul
Brazil	+ 2.7	Q1	+13.0	Jun	+ 6.8	Jul	+30.9	Jul	+ 7.9	Jun	49.8	Jun
Chile	+ 4.8	Q1	+ 5.1	Jun	+ 1.4	Jul	+ 6.7	Jul	– 0.1	Q1	15.9	Jun
Colombia	+ 4.1	Q1	+ 3.5	May	+ 6.2	Jul	+ 0.2	Apr	– 1.6	Q1	11.6	Jun
Mexico	+ 3.9	Q2	+ 5.2	Jun	+ 4.5	Jul	– 5.5	Jun	– 9.1	Q1	60.4	Jun
Peru	+ 3.0	Jun	+ 7.5	Jun	+ 4.6	Jul	+ 1.5	Jun	– 0.6	Q1	10.3	Jul
Venezuela	+29.8	Q1	+24.8	May	+21.8	Jul	+17.8	Q1	+12.3	Q1	18.9	May
Egypt	+ 3.1	2003†	+ 2.6	2003†	+ 5.5	Dec	– 6.7	Q1	+ 3.9	Q1	13.3	May
Israel	+ 3.0	Q2	+ 4.2	May	+ 0.5	Jul	– 5.3	Jul	+ 0.3	Q1	26.2	Jul
South Africa	+ 1.9	Q1	+ 4.9	Jun	+ 1.2	Jun	+ 0.3	Jun	– 2.0	Q1	10.3	Jul
Turkey	+10.1	Q1	+15.7	Jun	+ 9.6	Jul	–29.8	Jun	–12.1	Jun	33.9	Jun
Czech Republic	+ 3.1	Q1	+15.1	Jun	+ 3.2	Jul	– 2.3	Jun	– 6.0	Q1	26.3	Jul
Hungary	+ 4.2	Q1	+ 8.7	Jun	+ 7.2	Jul	– 4.2	Apr	– 7.1	Apr	12.8	Jul
Poland	+ 6.9	Q1	+15.7	Jun	+ 4.6	Jul	– 5.5	May	– 3.4	May	34.6	Jul
Russia	+ 7.4	Q1	+ 4.4	Jul	+10.4	Jul	+67.9	Jun	+38.4	Q2	84.9	Jul
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 6.8	Q1	+ 5.4	Jun	+ 4.1	Jul	– 2.3	May	– 1.1	Q1	1.3	Oct
Latvia	+ 8.8	Q1	+ 7.3	Jun	+ 6.7	Jul	– 2.5	Jun	– 1.4	Jun	1.5	Jun
Lithuania	+ 6.9	Q2	na		+ 1.9	Jul	– 2.9	Apr	– 1.5	Q1	3.2	Jun
Slovakia	+ 5.5	Q1	+ 4.7	Jun	+ 8.5	Jul	– 0.7	Jun	+ 0.1	Apr	11.9	Jun
Slovenia	+ 3.7	Q1	+ 9.6	Jun	+ 3.8	Jul	– 0.9	May‡	– 0.2	May	8.2	May
Pakistan	+ 5.1	2003†	+ 3.3	Mar	+ 8.5	Jun	– 3.4	Jul	+ 2.4	Q1	11.2	Jun
Saudi Arabia	+ 7.2	2003	na		+ 0.4	May	+61.2	2003	+29.7	2003	21.9	Jun

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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Financial markets

Aug 19th 2004
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Aug 18th		Dec 31st 2003	
	Aug 18th	year ago	Aug 18th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	15.1	3.50	1,425.3	– 1.9	– 9.2	– 9.2
Hong Kong	7.80	7.80	14.2	0.82	12,228.5	– 0.9	– 2.8	– 3.2
India	46.3	45.8	84.5	4.49	5,038.3	– 2.6	– 13.7	– 15.0
Indonesia	9,277	8,418	16,907	7.49	754.3	– 1.3	+ 9.0	– 1.0
Malaysia	3.80	3.80	6.93	2.87	809.6	– 1.4	+ 2.0	+ 2.0
Philippines	55.8	55.2	101.7	7.25	1,556.4	– 2.3	+ 7.9	+ 7.4
Singapore	1.71	1.75	3.12	1.13	1,890.7	– 0.3	+ 7.1	+ 6.4
South Korea	1,158	1,176	2,110	3.59	773.2	+ 2.7	– 4.6	– 1.9
Taiwan	34.0	34.3	62.0	1.10	5,427.8	+ 1.1	– 7.9	– 8.1
Thailand	41.5	41.6	75.6	1.56	605.3	+ 1.6	– 21.6	– 25.2
Argentina	3.02	2.90	5.50	5.38	952.8	– 0.4	– 11.1	– 13.7
Brazil	3.00	3.00	5.46	15.88	22,778.8	+ 5.6	+ 2.4	– 1.3
Chile	636	703	1,160	1.80	8,101.4	+ 1.9	+ 10.4	+ 2.8
Colombia	2,611	2,863	4,758	7.73	2,767.6	– 2.6	+ 18.6	+ 26.3
Mexico	11.3	10.8	20.7	7.13	10,080.6	+ 2.3	+ 14.6	+ 13.6
Peru	3.40	3.48	6.19	2.73	2,817.7	+ 0.7	+ 15.7	+ 18.1
Venezuela	2,699§	1,598	4,919	12.95	26,814.7	– 2.1	+ 20.8	+ 27.6
Egypt	6.19	6.15	11.28	11.13	16,510.2	+ 0.8	+ 41.9	+ 41.3
Israel	4.54	4.45	8.27	1.00	533.0	– 1.4	– 0.3	– 3.4
South Africa	6.52	7.40	11.9	7.50	10,687.3	+ 5.2	+ 2.9	+ 5.3
Turkey	1,469,000	1,396,000	2,677,253	23.88	19,268.1	+ 1.9	+ 3.5	– 1.1
Czech Republic	25.6	29.2	46.7	2.59	782.2	– 0.4	+ 18.7	+ 18.9
Hungary	201	233	366	11.01	11,927.7	+ 3.6	+ 27.2	+ 31.3
Poland	3.62	3.92	6.60	6.55	23,751.6	+ 2.2	+ 14.1	+ 17.9
Russia	29.2	30.3	53.3	13.00	546.1‡	+ 1.7	– 3.7	– 3.7
EMF (MSCI)*	1.00	1.00	1.82	na	425.8	+ 1.6	– 3.8	– 3.8
EMBI+†	1.00	1.00	1.82	na	304.0	+ 1.3	+ 3.1	+ 3.1

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Economist Intelligence Unit; Reuters; J.P. Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Akbank; Deutsche Bank

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